Audit Report

OFFICE OF THE INSPECTOR GENERAL

PRINCIPAL AND COMBINING FINANCIAL STATEMENTS OF THE DEFENSE BUSINESS OPERATIONS FUND - FY 1992

Report No. 93-134

June 30, 1993

Department of Defense

Acronyms

AFAA	Air Force Audit Agency
COD	Cost of Operations Division
DBOF	Defense Business Operations Fund
DeCA	Defense Commissary Agency
DFAS	Defense Finance and Accounting Service
DFSC	Defense Fuel Supply Center
DITSO	Defense Information Technology Services Organization
FMFIA	Federal Managers' Financial Integrity Act
GAO	General Accounting Office
JLSC	Joint Logistics Systems Center
OMB	Office of Management and Budget
SF	Standard Form
SGL	Standard General Ledger

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June 30, 1993

MEMORANDUM FOR SECRETARY OF DEFENSE
COMPTROLLER AND CHIEF FINANCIAL OFFICER OF THE DEPARTMENT OF DEFENSE

SUBJECT: Audit Report on the Principal and Combining Financial Statements of the Defense Business Operations Fund - FY 1992 (Report No. 93-134)

We are providing this audit report for your information and use, and for use by Congress. Financial statement audits are required by the Chief Financial Officers Act of 1990. Office of Management and Budget (OMB) Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993, requires the Inspector General to render an opinion on the fairness of financial statements. Also, we are required to report on the adequacy of internal controls and compliance with laws and regulations.

Although we were able to evaluate the internal controls and compliance with laws and regulations, we were unable to express an opinion on the financial statements. We are disclaiming an opinion on the Principal and Combining Statements because the statements provided to us were incomplete and because audit trails at three of the Defense Finance and Accounting Service Centers were judged by us to be inadequate. Also, accounting systems in place were not adequate to provide the needed information to prepare the financial statements. In addition, significant deficiencies in the internal control structure and noncompliance with required laws and regulations added to our inability to express an opinion. Also, neither the Comptroller of the Department of Defense nor the Director, Defense Finance and Accounting Service, provided us the required management representation letter. The failure of management to provide the letters also constitutes a limitation of scope sufficient to compel us to disclaim an opinion.

We identified several material weaknesses in the internal control structure of the Defense Business Operations Fund (DBOF). The material weaknesses in the internal control structure resulted in transactions that were not properly recorded or accounted for. The cash transactions could not be verified, and transactions made for or by others were not recorded in a timely manner. There were no eliminating entries or disclosures on \$17.7 billion of intrafund transactions. The financial statements were inaccurate because \$9.7 million of depreciation was not computed correctly, accounts receivable of \$222.0 million were not confirmed, revenue of \$274.0 million was not recognized, and liabilities of \$236.0 million were not properly accounted for. We were unable to ensure that assets were safeguarded against loss from unauthorized use because \$459.0 million of transactions recorded were not supported with adequate documentation. Also, capital assets and inventory of \$1.854 billion were variously overstated or understated on the financial statements because the valuation methods were not consistently applied throughout the DBOF business areas and physical inventories were not performed or reconciled to the financial records. We also determined that transactions were not executed in compliance with existing guidance. A lack of reconciliations for \$628.0 million resulted in inconsistencies between

reporting and financial presentation. The Weekly Flash Cash Reports developed to provide useful management information about cash flows were inaccurate. Audit trails of $2.409 billion of revenue, expenses and assets were inadequate for substantive testing, and there was a general lack of uniformity of accounting systems. Finally, the Standard General Ledger had not been implemented.

Our audit of compliance with laws and regulations that materially affected the reliability of the DBOF Principal and Combining Statements identified several instances of noncompliance. Accounting systems used for the DBOF were not in compliance with requirements of Title 2 of the General Accounting Office's "Policies and Procedures Manual for Guidance of Federal Agencies" and the Budget and Accounting Procedures Act of 1950. Financial statements prepared for the DBOF were not in full compliance with the Chief Financial Officers Act of 1990 as implemented by OMB Bulletin No. 93-02, "Form and Content of Agency Financial Statements," October 22, 1992. Reports to the Department of the Treasury required by the Debt Collection Act were inaccurate, and a system to monitor and report debts from contractors had not yet been implemented. A subaccount for recording and reporting capital asset transactions had not been established as required by the DoD Appropriations Act. New activities were added to the DBOF in violation of the Defense Authorization Act for FYs 1992 and 1993. Real properties, which by law are under jurisdiction of the Military Departments, were improperly reflected as assets on the financial statements.

Details of the weaknesses in internal controls and compliance with laws and regulations are discussed in Parts II and III of the report, respectively. This report contains no recommendations that are subject to resolution in accordance with DoD 7650.3; accordingly, comments are not required.

The courtesies extended to the audit staff are appreciated. If you have any questions on this audit, please contact Mr. F. Jay Lane, Program Director, at (703) 693-0430 (DSN 223-0430) or Mr. Kent E. Shaw, Project Manager, at (703) 693-0440 (DSN 223-0440). The planned distribution of this report is listed in Appendix E.

Robert J. Lieberman

Robert J. Lieberman
Assistant Inspector General
for Auditing

Office of the Inspector General, Department of Defense

Report No. 93-134 (Project No. 2FG-2008) June 30, 1993

AUDIT REPORT ON THE PRINCIPAL AND COMBINING FINANCIAL STATEMENTS OF THE DEFENSE BUSINESS OPERATIONS FUND - FY 1992

EXECUTIVE SUMMARY

Introduction. The Chief Financial Officers Act of 1990 requires an annual audit of funds such as the Defense Business Operations Fund (DBOF). The DBOF was established as a revolving fund in FY 1992 and consists of various DoD components. In FY 1992, the DBOF incorporated the revolving funds previously called the stock and industrial funds. In addition, the Defense Finance and Accounting Service, the Defense Commissary Agency, and three Defense Logistics Agency functions were added to the DBOF. Functional and cost management responsibilities rest with the Military Departments and Defense agencies. The Comptroller of the Department of Defense is responsible for the management of DBOF cash. Responsibility for the overall management of the DBOF is unclear. According to the accompanying financial statements, the total revenue for the DBOF for FY 1992 was $118.8 billion, total expenses were $118.7 billion, and total assets were $118.1 billion. Part IV, Appendix A, shows the reporting entities that comprise the DBOF.

Objectives. The overall objective of the audit was to determine whether the DBOF Principal and Combining Financial Statements for FY 1992 were presented fairly in accordance with generally accepted accounting principles for Federal entities. We evaluated the internal control structure and assessed compliance with applicable laws and regulations that could have a material effect on the financial statements. We also determined the usefulness of financial information reported to the Office of Management and Budget, the Department of the Treasury of the United States, the DoD, and the DBOF managers. In performing the audit, we relied heavily upon the work of the Service's audit organizations. Part IV, Appendix B, shows the extent of the work performed by others. Part IV, Appendix D, shows the organizations we visited or contacted.

Independent Auditor's Opinion. We are issuing a Disclaimer of Opinion on the financial statements. The financial statements provided to us on April 7, 1993, were incomplete. In addition, audit trails at three of the five Defense Finance and Accounting Service Centers were not adequate to enable transaction testing. Also, accounting systems in place were not adequate to provide the needed information to prepare the financial statements. In addition, significant deficiencies in the internal control structure and noncompliance with required laws and regulations added to our inability to express an opinion. Finally, we were not provided the necessary legal and management representation letters required by auditing standards for financial audits.

Internal Controls. Material internal control weaknesses existed. The material weaknesses in the internal control structure resulted in transactions that were not properly recorded or accounted for. Specifically, cash transactions could not be verified and transactions made for or by others were not recorded in a timely manner.

There were no eliminating entries or disclosures on intrafund transactions. The financial statements were overstated and understated because depreciation was not computed correctly, accounts receivable were not confirmed, revenue was not recognized, and liabilities were not properly accounted for. We were unable to ensure that assets were safeguarded against loss from unauthorized use because the transactions recorded were not supported with adequate documentation. Also, capital assets and inventory were overstated and understated on the financial statements because the valuation methods were not consistently applied throughout the DBOF business areas and physical inventories were not always performed or reconciled to the financial records. Finally, we determined that transactions were not executed in compliance with existing guidance. The lack of reconciliations resulted in inconsistencies between reporting and financial presentation. The Weekly Flash Cash Reports developed to provide useful management information about cash flows were inaccurate. Although audit trails were inadequate for substantive testing, there was a general lack of uniformity of accounting systems and the Standard General Ledger had not been implemented. Part II contains our report on internal control weaknesses identified.

Compliance with Laws and Regulations. Material instances of noncompliance with laws and regulations were disclosed. Accounting systems used for the DBOF were not in compliance with requirements of Title 2 of the General Accounting Office's "Policies and Procedures Manual for Guidance of Federal Agencies" and the Budget and Accounting Procedures Act of 1950. The DBOF Principal and Combining Financial Statements were not in full compliance with the Chief Financial Officers Act of 1990 as implemented by Office of Management and Budget Bulletin No. 93-02, "Form and Content of Agency Financial Statements," October 22, 1992. Reports to the Department of the Treasury required by the Debt Collection Act were inaccurate, and a system to monitor and report debts from contractors had not yet been implemented. A subaccount for recording and reporting capital asset transactions had not been established as required by the DoD Appropriations Act. New activities were added to the DBOF in violation of the Defense Authorization Act for FYs 1992 and 1993. Real properties, which by law are under the jurisdiction of the Military Departments, were improperly reflected as assets on the financial statements.

Usefulness of Financial Statements. The reliability and usefulness of the principal and combining statements are questionable. Although we could not ascertain the overall accuracy of the financial statements, we did note material weaknesses in the internal control structure and major discrepancies in cash balances reported on the financial statements with balances maintained by the Department of the Treasury. The footnotes, which are an integral part of the financial statements, were not included. Accordingly, the usefulness of the statements is in doubt. In any event, the audit will significantly improve the accuracy of future financial information and financial statements. Also, managers will have more accurate data for use in their decisionmaking processes.

Management Comments. We provided draft reports of Parts II and III to management on May 27, 1993. We received comments from the Acting Chief Financial Officer on June 17, 1993. Management generally agreed with the report, but took exception to our reportable conditions on inadequate audit trails in Part II and our reported instances of noncompliance with the Budget and Accounting Procedures Act, Title 2, Office of Management and Budget Bulletin No. 93-02, and the National Defense Authorization Act in Part III. Management comments are included in their entirety as Part VI of this report.

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This report was prepared by the Financial Management Directorate, Office of the Assistant Inspector General for Auditing, Department of Defense. Copies of the report can be obtained from the Secondary Reports Distribution Unit, Audit Planning and Technical Support Directorate (703) 614-6303 (DSN 224-6303).

Part I - Independent Auditor's Opinion on the Financial Statements

Introduction

The Defense Business Operations Fund (DBOF) was created by Congress on October 1, 1991, by combining Defense- and Service-owned revolving funds previously called the stock and industrial funds. In addition, the Defense Finance and Accounting Service (DFAS), the Defense Commissary Agency, and three Defense Logistics Agency functions (the Defense Technical Information Center, the Defense Utilization and Marketing Service, and the Defense Industrial Plant and Equipment Center) were added to the DBOF. Functional and cost management responsibilities rest with the Military Departments and Defense agencies. The Comptroller of the Department of Defense (DoD Comptroller) is responsible for the management of DBOF cash. Responsibility for the overall management of the DBOF is unclear. The DBOF reported revenues of $118.8 billion, expenses of $118.7 billion, and assets of $118.1 billion on its principal financial statements for 1992. Part IV, Appendix A, shows the reporting entities that comprise the DBOF.

The Chief Financial Officers Act requires an annual audit of revolving funds such as the DBOF. Preparation of the financial statements is the responsibility of the DFAS. Our responsibility is to express an opinion on those statements based on our audit.

Scope

We attempted to audit the Principal Statements and Combining Statements contained in the Annual Financial Statement of the Defense Business Operations Fund as of and for the year ended September 30, 1992. The Principal Statements were to include a Statement of Overall Financial Position, a Statement of Operations and Changes in Net Position, a Statement of Cash Flows, a Statement of Budget and Actual Expenses, and Notes to the Principal Statements.

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in financial statements, including accompanying Notes. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall Statement presentation. We developed client profiles for key management components of the DBOF and developed cycle memorandums that assessed the internal control structure for the Fund Balances with Treasury, capital and operating budgets, and the accounting systems. This financial statement audit was made during the period January 1992 through April 1993. In performing the audit, we relied heavily upon the work of the Service's audit organizations. Part IV, Appendix B shows the extent of the work performed by others. See Appendix D of Part IV for the organizations we visited or contacted. We believe that our audit efforts provide a reasonable basis for our audit results.

Limitations on scope impeded our attempt to audit the statements. We requested management and legal representation letters from the DoD

Comptroller, which also included a request for a management representation letter from the Director, DFAS. Because the legal representation letter from the DoD Comptroller and the management representation letter from the DFAS were not provided, there was a limitation of scope. Additionally, the financial statements provided to us were incomplete.

Auditing Standards

We conducted our audit in accordance with generally accepted auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, Department of Defense, and Office of Management and Budget Bulletin (OMB) No. 93-06, "Audits of Federal Financial Statements," January 8, 1993. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Principal and Combining Statements are free of material misstatements.

Accounting Principles

Accounting principles are currently being studied by the Federal Accounting Standards Advisory Board. Generally accepted accounting principles for Federal entities are to be promulgated by the Joint Financial Management Improvement Program principals, based on advice from the Board. In the interim, Federal agencies are to use a comprehensive basis of accounting as defined in OMB Bulletin No. 93-02, "Form and Content of Agency Financial Statements," October 22, 1992. The summary of significant policies included in the Notes to the Principal Statements, when provided by management, describes the accounting principles and methods of applying those principles that management has concluded are the most appropriate for presenting the DBOF's significant assets, liabilities, net position, results of operations, cash flows, and reconciliation to the budget.

Disclaimer of Opinion

We were not able to express an opinion on the financial statements for several reasons. The financial statements submitted to us were incomplete because the required Notes to the Financial Statements and the Supplemental Financial and Management Information were not provided. Such notes are integral parts of the financial statements and are necessary to ensure that the results of operations are fairly presented and fully disclosed. In addition, because there were inadequate audit trails at three of the Defense Finance and Accounting Service Centers and because accounting systems in place were not adequate to provide the needed information to prepare the financial statements, we do not believe that our audit attempt provides a reasonable basis for expressing an opinion on the Principal and Combining Statements of the Defense Business Operations

Fund as of September 30, 1992. (See Part II for a discussion of those weaknesses.) Furthermore, other significant deficiencies in the internal control structure and instances of noncompliance with required laws and regulations added to our inability to express an opinion. (See Parts II and III for details.) Also, a legal representation letter from the DoD Comptroller and a management representation letter from the DFAS were not provided to us as required by the auditing standards for financial audits. The failure of management to provide the letters constitutes in itself a limitation of scope sufficient to compel us to disclaim an opinion.

Additional Information

We also reviewed the financial information provided in the Overview to the Defense Business Operations Fund for FY 1992. Such information has not been audited by us; accordingly, we do not express an opinion on that information.

Part II - Internal Controls

Introduction

We audited the internal control structure of the Defense Business Operations Fund (DBOF) for the year ended September 30, 1992. Such audits are a requirement of the Chief Financial Officers Act of 1990 (the CFO Act), November 15, 1990.

Management of the DBOF is responsible for establishing and maintaining an internal control structure. In fulfilling this responsibility, estimates and judgments by management are required to assess the expected benefits and related costs of internal control structure policies and procedures. The objectives of an internal control structure are to provide management with reasonable but not absolute assurance that the following are met.

o Transactions are properly recorded and accounted for to permit the preparation of reliable financial statements and to maintain accountability over assets.

o Funds, property, and other assets are safeguarded against loss from unauthorized use or disposition.

o Transactions, including those related to obligations and costs, are executed in compliance with laws and regulations that could have a direct and material effect on the Principal Statements and, where applicable, Combining Statements, and any other laws and regulations that the Office of Management and Budget (OMB), entity management, or the Inspector General, Department of Defense, has identified as being significant for which compliance can be objectively measured and evaluated.

o Data that support performance measures are properly recorded and accounted for to permit preparation of reliable and complete performance information.

Objectives and Scope

The objective of the audit was to determine whether material internal control weaknesses existed. Specifically, we determined whether the internal control structure was established to ensure that the financial statements were free of material misstatements. We considered the internal control structure in determining audit procedures that were needed in order to express an opinion on the financial statements. We obtained an understanding of the internal control policies and procedures and assessed the level of control risk relevant to all significant cycles, classes of transactions, and account balances. For those significant control policies and procedures that had been properly designed and placed in operation, we performed sufficient tests to provide reasonable assurance that the controls were effective and working as designed. The tests were performed on events and transactions that occurred during FY 1992. For the purpose of this report, we have classified the significant internal control

objectives into the following categories: transactions properly recorded and accounted for, assets safeguarded against loss from unauthorized use, and transactions executed in compliance with existing regulations. Our consideration of the internal control structure included all of the categories. Our consideration of the internal control structure would not necessarily disclose all matters that might be reportable and, accordingly, would not necessarily disclose all conditions that are also considered to be material weaknesses. Conditions discussed will have a material effect on the FY 1992 DBOF Principal and Combining Statements.

In conducting the audit we relied upon the work of others. Financial statements of the individual DBOF business areas belonging to the Services were audited by auditors from the Military Departments whose reports have been furnished to us; therefore, our opinion, insofar as it relates to the amounts included for Service-owned business areas, with the exception of the Fund Balance with Treasury line item, is based solely on the reports of the other auditors. Those statements reflect total assets of $79.0 billion and total revenues of $69.8 billion for the period ended September 30, 1992. See Part IV, Appendix B, for the Summary of Audit Work Performed by Others.

We did not determine the reliability and completeness of the data used to support performance measures because the General Accounting Office (GAO) had announced an audit (GAO Code 918760) to evaluate the DoD's efforts to develop and implement performance factors. The Inspector General Act of 1978, Section 4(c) requires that we avoid such duplication of work with the GAO.

We conducted our audit in accordance with generally accepted Government auditing standards issued by the Comptroller General of the United States as implemented by the Inspector General, Department of Defense, and OMB Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the Principal and Combining Statements are free of material misstatements.

Prior Audit Coverage

The GAO reviews that included reportable conditions similar to the conditions we found are outlined here. In addition, we have reviewed prior audit coverage by the auditing entities of the DoD and the Military Services that reported similar internal control weaknesses discovered during the audits of the DBOF FY 1992 financial statements.

The GAO report, "Status of the Defense Business Operations Fund" (Report No. GAO/AFMD-92-79, OSD Case No. 9089-A), June 15, 1992, stated that key policies and systems necessary to run the DBOF in a businesslike manner have not been fully developed and implemented. Policies involving cash management, intrafund transactions, and capital asset accounting were needed but had not been finalized. In addition, accounting systems will not be fully

operational for another 3 years. The report made no recommendations; however, the GAO suggested that if Congress extended the DBOF beyond the April 1994 date called for in the National Defense Authorization Act for FYs 1992 and 1993, the DoD should not be permitted to add any new activities to the DBOF in FY 1994.

Another GAO report, "Immediate Actions Needed to Improve Army Financial Operations and Controls" (Report No. GAO/AFMD-92-82, OSD Case No. 8674-L), August 7, 1992, stated that a primary cause of the breakdown of internal control systems was the lack of sufficient commitment on the part of operational managers to first identify internal control weaknesses and then ensure the weaknesses were corrected within a reasonable period of time. The GAO identified weaknesses that it considered material but that were not reported by the Army in its Annual Statement of Assurance and, consequently, were not included in the Secretary of Defense's FY 1991 Annual Statement of Assurance. The weaknesses the GAO identified included failure to investigate or resolve abnormal and unusual account balances; failure to reconcile differences between general ledger and detailed records; and failure to monitor accuracy of the inventory records. Recommendations included clarifying responsibilities for accuracy of financial data; ensuring that expertise and resources are available to accomplish financial management improvement projects; identifying changes needed to improve the accuracy of existing accounting systems; ensuring consistency of accounting policies and practices and their applications; and ensuring compliance with existing asset control procedures. Of the report's 30 recommendations, the Acting Comptroller of the Department of Defense concurred with 19, partially concurred with 9, did not concur with 1, and was still reviewing 1 when the report was issued.

The GAO report, "Examination of the Army's Financial Statement for Fiscal Year 1991" (Report No. GAO/AFMD-92-83, OSD Case No. 8674-M), August 7, 1992, stated that tests of internal controls affecting or potentially affecting the Army's Principal Statements showed the internal controls could not be relied upon to achieve their intended objectives. The GAO identified material weaknesses not reported by the Army in the Annual Statement of Assurance; however, the Army nonconcurred, stating that the areas needing additional management attention did not materially affect the Statement. The disagreement reflects a difference of opinion between the Army and the GAO on what constitutes materiality. The large overall number of internal control weaknesses prevented the GAO from expressing an overall opinion on the Army's Principal Statements.

The GAO report, "Financial Audit: Aggressive Actions Needed for Air Force to Meet Objectives of the CFO Act" (Report No. GAO/AFMD-92-12, OSD Case No. 8376-L), February 19, 1992, noted pervasive internal control weaknesses throughout the Air Force that resulted from failure to follow established procedures for reviewing accounts for abnormal balances and for reconciling control accounts with subsidiary accounts and supporting records. The GAO recommended reconciling disbursements with obligations and promptly correcting errors, and documenting adjustments to subsidiary records and control accounts. The GAO also suggested that internal control problems

both with reconciliations and with inadequate documentation for adjustments be included in future Federal Managers' Financial Integrity Act (FMFIA) reports.

The GAO report, "Financial Audit: Air Force Does Not Effectively Account for Billions of Dollars of Resources" (Report No. GAO/AFMD-90-23, OSD Case No. 8193-A), February 23, 1990, stated the Air Force has significant internal control weaknesses. By not performing reconciliations and by making unsupported adjustments, the Air Force lost accountability and the opportunity to determine and address the causes of possible instances of mismanagement, fraud, or abuse. The GAO recommended improving the accuracy of existing financial information, performing reconciliations, and documenting adjustments. The Comptroller of the Department of Defense (DoD Comptroller) concurred with the recommendations. The GAO did not express an opinion on the Air Force's financial statements because of the existing conditions.

The GAO report, "Financial Management: Navy Industrial Fund Has Not Recovered Costs" (Report No. GAO/AFMD-93-18, OSD Case No. 9287), March 23, 1993, stated that the DoD had not developed a cash management policy. The GAO recommended a cash management policy be developed to prescribe the minimum and maximum amounts of cash the DBOF needs to operate. According to the report's Executive Summary, management comments were not obtained at the request of the Chairman, Subcommittee on Readiness, Committee on Armed Services, House of Representatives.

Audit coverage by the Department of Defense and the Services included the following.

The Air Force Audit Agency (AFAA) report, "Report of Audit on the Management of Budget Clearing Accounts" (Project No. 9265314), May 24, 1990, found the internal controls were not adequate to ensure compliance with established procedures. Some budget clearing accounts were not certified semiannually as required and balances had remained in suspense accounts for periods in excess of 1 year because controls and reconciliations were not effectively implemented. Recommendations included establishing controls to monitor the receipt of the semi-annual certifications; establishing procedures to age clearing account balances; and following up on overaged accounts. Management concurred and revised Air Force regulations to correct the weaknesses noted.

Results of Audit

Internal control weaknesses existed that we consider to be material and reportable under standards established by OMB Bulletin No. 93-06. Reportable conditions are matters coming to our attention relating to significant deficiencies in the design or operation of the internal control structure that, in our judgment, could adversely affect the organizations' ability to effectively control and manage its resources and ensure reliable and accurate financial information to manage and evaluate operational performance. A material weakness in the internal control structure is a reportable condition in which the design or

operation of one or more of the elements of the internal control structure does not reduce, to a relatively low level, the risk that errors or irregularities may occur. Such errors would be in amounts that would be material in relation to the financial statements being audited or material to a performance measure or aggregation of related performance measures, and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Transactions Not Properly Recorded and Accounted For. We were unable to determine if transactions were properly recorded and accounted for due to the following conditions.

Controls Over Cash Inadequate. We could not verify cash balances on the DBOF FY 1992 Consolidating, Combining, and Business Area Financial Statements because three of the five Defense Finance and Accounting Service (DFAS) Centers were using improper accounting procedures. Additionally, we identified a material discrepancy between cash balances reported by the DBOF and Department of the Treasury (Treasury) records.

We could not confirm the DBOF cash transactions reported by the DFAS-Denver Center because accounting procedures used did not provide adequate separation of suspense account transactions made for the DBOF from transactions made for the Air Force General Fund (appropriation account no. 57X6875). Those procedures resulted in comingling of the DBOF transactions with Air Force transactions. The reported balance in the overall Air Force suspense account for FY 1992 was $6.508 billion in collections and $6.494 billion in disbursements; however, the DBOF portion of those transactions could not be determined. We originally reported $614.0 million in collections and $633.0 million in disbursements in our draft report. Those amounts were only the monthly totals. The updated figures are annual amounts. In addition, we found that the DFAS-Denver Center, on occasion, improperly reported estimates of its transactions rather than actual totals on the Statements of Transactions (DD Form 1329) forwarded to the Treasury. Responsible managers at the DFAS-Denver Center stated that they used an estimate of cash transactions whenever they had not received the required transaction information from its disbursing offices in time to prepare their report to the Treasury. The use of estimates for these reports is not authorized by DoD or Treasury guidance and does not provide an accurate assessment of cash transactions.

Accounting procedures used by the DFAS-Indianapolis Center and the DFAS-Cleveland Center precluded net disbursements, totaling $14.3 million and $26.0 million, respectively, from being identified to the proper DBOF business areas.

We also found a material discrepancy in year-end cash balances between DBOF financial statements and Treasury records. According to "DoD Guidance on Form and Content of Financial Statements for FY 1992 Financial Activity," December 30, 1992, the cash balances at the consolidating and business area levels should equal the difference between cash disbursements and cash collections during the fiscal year. We identified a variance of approximately $649 million between what the Treasury reported as a reduction to the DBOF

appropriation ($3.160 billion) and what the business area financial statements reported as cash balances on the Fund Balance with Treasury account ($2.511 billion). Likewise, there was about a $649 million variance in what the Treasury reported as Current Year Appropriations at the end of FY 1992 ($7.295 billion) and what the DBOF Combining Statements presented as Fund Balance with Treasury, Departmental ($6.646 billion). We were able to trace the discrepancy of about $649 million to four business areas:

- o Army Supply Management
- o Air Force Supply Management
- o Defense Supply Management
- o Navy Distribution Depot

At the conclusion of our audit field work, we still had not determined the cause of the discrepancies.

Transactions For and By Others Not Recorded in a Timely Manner. Timing differences in recording transactions resulted in variances between records of the DFAS Centers and the business areas. The financial statements for each business area must exclude Transactions For Others and include Transactions By Others. The transactions for and by others are not recorded at the business area level until the transactions have been reviewed and accepted. This lag in reporting causes discrepancies between financial data at the DFAS Centers and operating data at the business areas and results in "unmatched" buyer and seller transactions, unliquidated obligations, and undistributed balances. The variances overstate accounts receivable and understate accounts payable at the business areas. We found subsidiary records did not support $2.95 billion of unliquidated obligations recorded in the Defense Fuel Supply Center (DFSC) trial balance portion of the Defense Logistics Agency Supply Management business area. The DFAS and the DFSC did not ensure the accuracy and completeness of the recorded obligations. Also, the subsidiary records were not available in sufficient detail to support $492.7 million of undistributed disbursements and $356.1 million of undistributed collections.

Elimination or Reporting of Intrafund Transactions Not Performed. Approximately $17.7 billion of intrafund transactions among business areas of the DBOF are not properly identified or eliminated from the FY 1992 DBOF Combining or Consolidated financial statements. This is a result of the lack of specific DBOF controls and policies regarding the treatment of those transactions. In addition, the present accounting systems used to record disbursements and collections are not designed to identify and retain the intrafund data when both the buyer and seller are DBOF activities. Due to the lack of guidance and inadequate accounting systems, we were unable to determine what amount of intrafund transactions should have been eliminated or disclosed in the DBOF financial statements. The DoD Comptroller estimated $17.7 billion in intrafund transactions for the DBOF during FY 1992.

Depreciation Computations Incorrect. Depreciation schedules had not been developed for capital assets throughout the reporting entities. This caused many of the entities to incorrectly report depreciation. The DoD Manual 7220.9-M, "DoD Accounting Manual," as amended, June 17, 1991, prescribes depreciation guidance and subsequent policies and procedures included in the DoD Comptroller's memorandum on "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992. That guidance requires that depreciation be computed using the straight-line method. The straight-line method is based on the original acquisition cost or reasonable estimate divided equally among accounting periods during the asset's useful life. For example, Army Depot Maintenance personnel did not accurately compute depreciation of the fixed assets, both because the personnel recorded incorrect information and because personnel did not have an accounting system that allowed them to compute depreciation. The Air Force Depot Maintenance business area did not depreciate capital assets at their useful lives because Air Force depreciation policy did not agree with the guidance memorandum issued by the DoD Comptroller. As a result, the Air Force Depot Maintenance depreciation was understated by $9.7 million.

Accounts Receivable Not Confirmed and Revenue Not Recognized. Accounts receivable and revenue balances were misstated due to inaccurate accounting entries and lack of controls in place to properly record those entries. Specifically, the Air Force Depot Maintenance business area did not recognize at least $274.0 million in revenue associated with work completed as of September 30, 1992. It also had inaccurate journal voucher entries of $221.0 million to the accounts receivable and the progress billings account. Also, the Air Force Transportation business area revenue was not always processed for billing. The AFAA found that about $9.6 million of revenue earned for the movement of passengers, cargo, and mail on established routes was not billed. Finally, the Air Force Base Support accounting controls were not in place to record revenue and receivable transactions in the correct accounting period. As a result, revenue of $7.2 million and accounts receivable of $1.2 million may be materially misstated.

Liabilities Not Properly Accounted For. Liabilities of the DBOF were misstated due to the lack of accounting controls and the failure of accounting personnel to follow the DoD Manual 7220.9-M. The Navy's Military Sealift Command business area had estimated invalid accruals of $38.1 million for charter hire, $145.2 million for cargo, and $38.1 million for supplies and services. The invalid accrual amounts were accrued in the wrong year, not adequately liquidated, and improperly written off. Additionally, the AFAA found that the Fuel Division of Air Force Supply Management purchases and its disbursements to foreign governments were not properly accounted for. The Air Force Fuel Division did not record or pay for fuel purchases away from home and did not report $3.9 million of off-station fuel purchases in the periods when the transactions occurred. Also, the Air Force Base Support did not reconcile accounts payable balances to unpaid bills. The payroll accrual procedures did not ensure accurate recording of payroll transactions or correct adjusting entries for payroll expenses to actual amounts. Also, accounting controls were not in place for recording all valid payroll transactions in plant financial records and reporting payroll transactions in the correct accounting

periods. As a result, $6.6 million in payroll and related accrued liabilities of payables could not be substantiated.

Assets Not Safeguarded Against Loss From Unauthorized Use. We were unable to ensure that assets are safeguarded from unauthorized use.

Lack of Supporting Documentation. Our substantive testing on the Fund Balance with Treasury account identified a lack of supporting documentation. The DoD Directive, 5015.2, "Records Management Program," March 22, 1991, requires the DoD Components to establish and maintain a central Records Management Program to ensure that DoD records are maintained and managed from creation through disposal. We determined subsidiary records were not available to support adjustments of $2.74 billion in the DFSC Statement of Cash Flows and $1.14 billion of other unfunded expenses in the DFSC's Statement of Budget and Actual Expenses. Army Transportation business area accounts receivable balances of about $23.7 million did not have supporting documentation, and the accounts payable subsidiary ledger incorrectly contained debit balances of about $112.0 million with no documentation to support the recorded entries. Furthermore, the Army Transportation business area financial statement contained $28.0 million of unsupported adjustments. The Navy's Military Sealift Command could not adequately support transactions of $29.2 million for maintenance and repair and other per diem items, $74.0 million for cargo, and $191.7 million for supplies and services. Managers of the Air Force Supply Management business area made adjusting entries totaling $75.0 million and the Fuel Division of Supply Management paid fuel vouchers totaling $6.8 million without required supporting documents. As a result, the $167.0 million in accounting adjustments or the related account balances reported in the Air Force financial statements were not substantiated. The AFAA also found that the Air Force Depot Maintenance business area made incorrect or unsupported entries totaling $112.2 million to year-end contract inventory accounts on the financial statements because Depot Maintenance had not established effective procedures for making adjusting entries. As a result, the $848.3 million of Inventory Not Held For Sale could not be substantiated on the Air Force Depot Maintenance Statement of Financial Position.

Capital Asset and Inventory Not Valued Correctly and Existence Uncertain. The valuation methods of reporting assets and inventory on the DBOF financial statements were not consistently applied throughout the business areas. Also, physical inventories were not always performed or reconciled to the financial records. The DoD Manual 7220.9-M requires physical inventories of personal property to verify the existence of property recorded in general ledger accounts and provides detailed guidance on reconciling general ledger inventory accounts to subsidiary property records. The DoD Manual 7220.9-M also provides criteria for capitalizing assets; however, the threshold for asset capitalization has been increased to $15,000 by the "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992. The DoD 7200.14-M, "Department of Defense Accounting and Reporting of Government Property Lost, Damaged, or Destroyed," May 16, 1977, also provides procedures for reconciling differences as a result of physical counts. We found that the DFAS Centers did not

reconcile and match the physical inventory to the financial records for capital assets. Also, we found the property, plant and equipment account classification presented on the DFAS business area financial statements was understated by $13.3 million. In addition, the Defense Commissary Agency (DeCA) Resale Stocks business area did not ensure that approximately $800.0 million of inventory recorded on the general ledger agreed with the subsidiary ledgers.

The Army Depot Maintenance business area did not properly capitalize $87.2 million of fixed assets. Assets and liabilities were overstated by $70.0 million and $4.0 million, respectively, because two depot activities were included in the FY 1992 statements even though they are no longer Army Depot Maintenance activities. The Navy's DBOF fixed assets recorded in the financial statements could not be located. The DBOF inventory records were inaccurate, and some fixed assets were not recorded in the financial statements. The fixed assets that were reported on the financial statements were capitalized in error or in the wrong amount and often were not removed from the financial statements after disposal or transfer. As a result, the Navy's Consolidated Statement of Financial Position was understated by $177.5 million. The Air Force Base Support business area did not accurately record, capitalize, and value fixed assets. As a result, the $5.7 million fixed asset balance may be materially misstated.

The Army Depot Maintenance business area did not properly account for materiel inventories valued at about $332.4 million because of inaccurate costing methods and poor record keeping. Also, about $84.8 million in in-transit inventories reported in the financial statement may be invalid because the transactions were old and supporting documentation was difficult to find. Additionally, the Army Transportation inventories were valued at the latest acquisition price. The Navy DBOF physical inventories were not conducted, or, when conducted, were incomplete. The Navy DBOF unused materiel was not returned to the appropriate inventory account or recorded on financial records, and stock levels were not always reviewed for excesses. As a result, the Department of the Navy's DBOF Consolidated Financial Statements contained $153.0 million in gross inventory misstatement.

Transactions Not Executed in Compliance with Existing Guidance. We identified the following conditions that were not in compliance with existing guidance.

Lack of Reconciliation. Financial data were not reconciled to ensure consistent reporting of the same information. The August 19, 1991, "Fiscal Year 1992 DBOF Financial Management Guidance," issued by the DoD Comptroller, stated that disbursement and collection reports shall be reviewed and reconciled to the Statement of Transactions before being submitted to the next reporting level. Each DFAS Center's divisions and branches are responsible for specific reports; however, we could not identify one reporting division or branch at the DFAS Centers performing any form of reconciliation with the Statement of Transactions, or with another reporting division or branch, before or after the information is transmitted to the Treasury. This condition results in inconsistencies between cash reporting and financial presentation. During our visits to the DFAS Centers, we determined that no

reconciliations of Fund Balances with Treasury were performed in FY 1992, which resulted in an unreconciled difference of $15.8 million between the DFAS Statement of Financial Position and the General Ledger. We found the DFSC did not coordinate with the DFAS to ensure that financial data was accurate. The DFSC internal management control reviews required by the FMFIA did not determine whether subsidiary ledger accounting records were periodically verified to supporting documentation, did not properly track and report material weaknesses, and had not established procedures to describe the coordination between the DFSC and the DFAS.

Unreliable Weekly Flash Cash Reports. The Weekly Flash Cash Reports cannot be relied on to evaluate cash working cycle needs of the DBOF. A requirement to prepare DBOF Weekly Flash Cash Reports was implemented to aid management in determining what the cash needs should be for a given time frame. We determined that feeder reports from the business areas did not agree with reports submitted to the DoD Comptroller by the DFAS-Cleveland Center, Defense Accounting Office, Arlington, Virginia. Even though the DBOF business areas were providing Weekly Flash Cash Reports, the reports were not reconciled and included estimates and inaccuracies that rendered them useless for management cash flow decisions.

Inadequate Audit Trails. The audit trails were not sufficient to trace or vouch transactions at the sites visited. The Joint Financial Management Improvement Program's publication, "Core Financial System Requirements," January 1988, requires that systems provide audit trails that trace transactions from source documents through successive levels of summarization to the financial statements. The audit trail should also be traceable in reverse. The accounting systems at the DFAS Centers in Columbus and Indianapolis do not include document or voucher numbers for DBOF transactions. The DFAS Centers report DBOF cash transactions to the Treasury based on feeder information from disbursing offices of each Military Department. For example, at the DFAS-Indianapolis Center, the data is summarized by the disbursing offices and batch processed (daily by the Air Force and weekly for all other Services) to the DFAS Center with a batch number reference instead of a document or voucher number. A sample of 50 summarized transactions selected from the DFAS-Indianapolis Center's accounting system included more than 7,000 detailed transactions. The detailed transactions are stored on microfiche organized by disbursing office, then by appropriation. The lack of an audit trail made the verification of account balances difficult at the audit sites. The Air Force Transportation business area did not have a system in place to accurately capitalize property, plant and equipment. In addition, due to an incomplete audit trail, the AFAA was unable to substantiate $1.07 billion of revenue derived from the movement of passengers, cargo, and mail on established routes; $998.9 million of military personnel expenses; and $339.9 million of property, plant and equipment at the Air Force Transportation business area. Also, disbursements of $546.0 million were made to commercial carriers without evidence from the carriers that the services were rendered.

Lack of Uniform Accounting Systems. The accounting systems in use by the DFAS Centers do not provide consistency in financial reporting or comparability of information on operations for the DBOF. The CFO Act

requires an agency Chief Financial Officer to develop and maintain an integrated agency accounting and financial management system. Such systems are to provide for complete, reliable, consistent, and timely information prepared on a uniform basis and responsive to the financial information needs of agency management. The DFAS Centers are using existing accounting systems to provide Service-unique information, while the DBOF reporting requirements are the same for each Service. Each of the DFAS Centers has developed unique computer programs to summarize information for reporting to the DBOF. The summarized information must be collected from several Service-unique sources, which results in a further lack of comparability for data received for the DBOF from the DFAS Centers.

The DeCA did not have an effective reporting system that systematically summarized financial information. We found no documented procedures for the DFSC to determine which general ledger accounts were used to develop the various account classifications on the financial statements. We determined that DFAS personnel had to crosswalk Defense Logistics Agency general ledger accounts to the DoD uniform chart of accounts, then crosswalk the DoD accounts to the account classifications on the financial statements. The integrated general ledger systems of the Army's Depot Maintenance and Transportation business areas were not used to produce the Army's FY 1992 financial statements. Instead, reports from the Departmental Budget and Reporting System were relied on for preparing financial reports. Similarly, the Air Force Transportation business area did not have a fully integrated double-entry accounting system. Information was gathered from automated and manual systems to create a consolidated general ledger. The procedures used to create this general ledger were not documented, and there was no assurance that all transactions were recorded. The Air Force Supply Management automated accounting system was not in place to collect and report expenses as required and the accounting systems did not generate sufficient and suitable accounting data to permit the review and certification of FY 1992 financial statements. Those conditions exist because the Standard General Ledger accounts have not been incorporated into the DFAS accounting systems.

Lack of Standard General Ledger. The U.S. Government Standard General Ledger (SGL) has not been fully implemented by the DFAS for the DBOF business areas as required by Title 2, "Accounting" of the GAO's "Policy and Procedures Manual for Guidance of Federal Agencies." We identified at least seven different general ledger structures in use by DBOF activities. The SGL is intended to standardize Federal accounting and to meet the basic Federal financial statement and budget execution reporting requirements. The Military Departments and the DoD Components are using Service-unique charts of accounts and are crosswalking the financial data from the activities' general ledger accounts to the SGL for preparation of management reports and financial statements. The lack of a uniform general ledger structure within the DBOF unnecessarily increases the potential for accounting errors and increases the level of effort required to prepare routine reports for the use of other Government parties, such as the Treasury and the OMB, and to audit the financial statements. Since the crosswalks in use do not always have a one-for-one relationship to the SGL, transactions are not properly recorded and accounted for to permit the preparation of reliable financial

statements and to maintain accountability over assets. In addition, the general ledger accounts in use at the DFAS Centers do not adequately record the level of detail required in the DoD Comptroller memorandum, "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992. In FY 1992, only one of the DBOF activities, the DeCA Resale Stocks business area, used the DoD Uniform Chart of Accounts, which is equivalent to the SGL. The Defense Information Service Agency Information Services business area has contracted with the accounting firm of KPMG Peat Marwick to convert its accounting system to the SGL for FY 1993.

Management Comments

We received comments on June 17, 1993, from the Acting Chief Financial Officer of the Department of Defense. Management generally concurred with the material weaknesses identified in our report; however, management disagreed with our comments about an inadequate audit trail. Management stated the individual transactions retain an audit trail through the first level of summarization and that each level of consolidation retains an audit trail.

Management disagreed with parts of our comments on inadequate controls over cash. Management believed the $649 million variance between net disbursements reported by the Treasury and net disbursements reported on the financial statements was a misstatement of fact.

Management agreed in principle with our comments on the incorrect depreciation computations, but noted the $9.7 million understatement in the Air Force Depot Maintenance area was merely 1.2 percent of the total depreciation expense for the DBOF.

Management agreed in principle on the lack of uniform accounting systems, but suggested there was no evidence that the DFAS Centers did not prepare the financial statements correctly. The complete text of management's comments is at Part VI.

Audit Evaluation of Management Comments

We believe that audit trails should be maintained in such a way that the auditors can identify individual transactions and select samples in a timely manner to perform an audit within a limited time frame. The progressive summarization of detail may be efficient for operations; however, individual transaction identification is necessary for substantive testing. If audit trails are not sufficient to collect reliable and relevant evidence, we cannot render an opinion on the financial statements as a whole.

We determined that the total dollars transferred to the DBOF and transfers from the DBOF to other appropriations during FY 1992 resulted in an overall available DBOF balance of $7.295 billion. We agree that the $4.135 billion Fund Balance with Treasury is what the Treasury reported as a balance for September 30, 1992. Table 1 summarizes the transactions affecting the DBOF appropriation during FY 1992.

Table 1. DBOF Appropriations Available for FY 1992 and Fund Balance with Treasury as of September 30, 1992 (in millions)

Initial Transfer to DBOF from Existing Stock and Industrial Funds	$6.494
FY 1992 Appropriation Provided to DBOF	3.424
Funds Transferred from DBOF as Directed by Congress	(2.575)
Transferred from DBOF for Lease Payment	(0.048)
Total DBOF Appropriations Available for FY 1992	$7.295
Net Disbursements Reported to Treasury and OMB	(3.160)
Fund Balance with Treasury as of September 30, 1992	$4.135

Our discussion of the variance in reported disbursements was factual. The net disbursements recorded on the Combining Financial Statements were $2.511 billion for FY 1992. The net disbursements of $3.160 billion were reported by the DFAS to the OMB for FY 1992. Table 2 shows the variance between the net disbursements reported on the Combining Financial Statements and to the OMB.

Table 2. Variance Between Net Disbursements Reported on Combining Financial Statements and Net Disbursements Reported to the OMB

Consolidated Business Areas	Reported on Combining Financial Statements (millions)	Reported to the Office of Management and Budget (millions)	Variance (millions)
Army	($1,070.3)	($1,253.7)	($183.4)
Navy	272.2	364.6	92.4
Air Force	(1,172.4)	(1,972.1)	($799.7)
Defense Agencies	(399.0)	(157.0)	242.0
DISA	50.4	50.4	
DFAS	120.9	120.9	
DeCA	(298.8)	(298.8)	
Joint Logistics	(14.3)	(14.3)	
Total	($2,511.3)	($3,160.0)	($648.7)

The variance of about $649 million was acknowledged by the DFAS-Cleveland Center, Defense Accounting Office, Arlington, Virginia, by adjustments to three Supply Management business areas and one Distribution Depot business area.

Regarding the Acting CFO's comment on the $9.7 million depreciation computation error, it should be noted that we did not determine the overall net error in depreciation computations for the DBOF, and the $9.7 million error is merely one example. Furthermore, even though the $9.7 million in depreciation was only 1.2 percent of DBOF overall, the understatement of depreciation was 10 percent of the Air Force Depot Maintenance business area's depreciation expense. We agree, however, that other problems and weaknesses discussed in this report resulted in much greater distortions to the Principal and Combining Financial Statements.

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Part III - Compliance with Laws and Regulations

Introduction

We tested the Principal and Combining Statements of the Defense Business Operations Fund (DBOF) for material instances of noncompliance with laws and regulations for the year ended September 30, 1992. Such tests are required by the Chief Financial Officers Act (CFO Act), November 15, 1990.

Objectives and Scope

The objective of the audit was to determine whether material instances of noncompliance with laws and regulations existed. Material instances of noncompliance are failures to follow requirements of, or violations of prohibitions contained in laws and regulations. Such failures or violations are those that cause us to conclude that the aggregation of the misstatements resulting from those failures or violations is material to the Principal and Combining Statements, or those whose sensitive nature would cause them to be perceived as significant by others.

Compliance with laws and regulations applicable to the DBOF is the responsibility of DBOF managers. To ensure that the DBOF Principal and Combining Statements were free of material misstatements, we tested compliance with laws and regulations that may directly affect the financial statements and certain other laws and regulations designated by the Office of Management and Budget (OMB) and the DoD. The laws and regulations tested are identified in Part IV, Appendix C.

The following key laws and regulations were not tested during the audit due to resource constraints.

- Federal Employees' Compensation Act of 1916
- Civil Service Retirement Act of 1930
- Fair Labor Standards Act of 1938
- Federal Employees Health Benefits Act of 1959
- Civil Service Reform Act of 1978
- Federal Employees' Group Life Insurance Act of 1980
- Federal Credit Reform Act of 1990

As part of our audit, we reviewed management's process for evaluating and reporting on internal control and accounting systems as required by the Federal Managers' Financial Integrity Act (FMFIA) and compared the agency's most recent FMFIA reports with the evaluation we conducted of the entity's policies, procedures, and systems for documenting and supporting financial, statistical,

and other information presented in the Overview of the Reporting Entity and Supplemental Financial and Management Information. Our objective, however, was not to provide an opinion on overall compliance with such provisions.

We conducted our audit in accordance with generally accepted Government auditing standards, issued by the Comptroller General of the United States as implemented by the Inspector General, Department of Defense, and OMB Bulletin No. 93-06, "Audit Requirements for Federal Financial Statements," January 8, 1993. Those standards require that we plan and perform the audit to obtain reasonable assurance that the DBOF Principal and Combining Statements are free of material misstatements.

Prior Audit Coverage

The DBOF was established on October 1, 1991. Since then, several reports have been issued by the Inspector General, Department of Defense; the General Accounting Office (GAO); and the Service agencies regarding debt collection, compliance with the Prompt Payment Act, Antideficiency Act violations, and DBOF implementation procedures.

The Office of the Inspector General, Department of Defense, Report No. 92-021, "Debt Collection and Deposit Controls," December 13, 1991, stated the DoD Components had not implemented prompt or aggressive collection strategies to pursue delinquent payments and that the policies and procedures for collecting delinquent debt were not consistent with Federal laws and regulations. The Inspector General, Department of Defense, recommended that the Defense Finance and Accounting Service (DFAS) centralize control over the DoD's debt collection and develop uniform operating procedures. The DFAS concurred and began implementing the recommendations.

The Office of the Inspector General, Department of Defense, issued Report No. 92-088, "Defense Agencies' Compliance with Prompt Payment Procedures," May 8, 1992, and Report No. 93-071, "Consolidated Report on the DoD Wide Audit of Compliance with Prompt Payment Procedures," March 22, 1993. The objective of both audits was to determine whether bills were being paid in accordance with the provisions of the Prompt Payment Act, OMB Circular A-125, "Prompt Payment," August 19, 1982, and the DoD Manual 7220.9-M, "DoD Accounting Manual," as amended, June 17, 1991. The results of the audits showed internal controls were not being implemented as required by the FMFIA and material internal control weaknesses existed in payment operations, including control of supporting documents and records. Management concurred with the recommendations to ensure that material internal control weaknesses in payment operations were reported in the Annual Statements of Assurance.

The Assistant Inspector General for Audit Policy and Oversight issued the "Survey Report on the Review of Processing of Violations of the Antideficiency Act," on July 31, 1991. The objective of the review was to evaluate the adequacy of policy and procedures for processing potential and apparent

violations of the Antideficiency Act at the Office of the Comptroller of the Department of Defense (DoD Comptroller), the Military Departments, and selected field organizations. The review showed that the decentralized administrative processing of potential and apparent violations of the Antideficiency Act has resulted in untimely reporting of violations to the President and the Congress. The review showed that violators of the Antideficiency Act are given mild penalties for either the violations or failure to report them in a timely manner.

Results of Audit

Our audit disclosed several instances of noncompliance with laws and regulations that materially affected the reliability of the DBOF Principal and Combining Statements. Accounting systems used for the DBOF were not in compliance with requirements of Title 2, "Accounting" of the GAO's "Policy and Procedures Manual for Guidance of Federal Agencies" and the Budget and Accounting Procedures Act of 1950. Financial statements prepared for the DBOF were not in full compliance with the CFO Act as implemented by OMB Bulletin No. 93-02, "Form and Content of Agency Financial Statements," October 22, 1992. Reports to the Department of the Treasury (Treasury) required by the Debt Collection Act were inaccurate; and a system to monitor and report debts from contractors had not yet been implemented. A subaccount for recording and reporting capital asset transactions had not been established as required by the Department of Defense Appropriations Act, 1992. New activities were added to the DBOF in violation of the Defense Authorization Act for FYs 1992 and 1993. Real properties, which by law are under the jurisdiction of the Military Departments, were improperly reflected as assets on the financial statements.

Budget and Accounting Procedures Act of 1950 and GAO Title 2. Accounting systems for the DBOF do not meet accounting system requirements of Title 2 of GAO's "Policy and Procedures Manual for Guidance of Federal Agencies." Under the Budget and Accounting Procedures Act, the head of each Federal agency is responsible for establishing and maintaining adequate systems of accounting and internal controls. The Act also requires that those systems conform to the accounting principles, standards, and related requirements prescribed by the Comptroller General. Appendix III to Title 2 prescribes accounting system standards and requirements that agency heads must observe in establishing, maintaining, and reporting on their systems of accounting and internal controls. That includes a requirement that accounting systems be maintained on an accrual basis and use the United States Standard General Ledger Chart of Accounts and meet "Core Financial System Requirements" of the Joint Financial Management Improvement Program, January 1988. The systems must incorporate adequate audit trails and double-entry accounting. Further, systems should include, for each appropriation or fund, accounts that provide appropriation records on obligations incurred and liquidated to assist in controlling expenditures and disbursements and in reporting the status of appropriations and funds. Our audit identified material instances where accounting systems were not in compliance with those requirements. Those

instances of noncompliance are discussed in detail in Part II, Internal Controls, sections on Lack of Standard General Ledger, Inadequate Audit Trails, and Lack of Uniform Accounting Systems. Additionally, we found that the DFAS did not disclose the value of the use of the facilities at three of the five DFAS Centers (which we estimated to be $27.0 million) as required by Title 2. The Centers were provided to the DFAS at no cost in FY 1992.

Chief Financial Officers Act of 1990. The Office of the DoD Comptroller did not fully comply with OMB Bulletin No. 93-02, which implements the CFO Act. The financial statements were not submitted to the Director, OMB, by the required date, and the financial statements were incomplete. We believe that several factors contributed to the late and incomplete submission of the financial statements.

o Many of the DFAS personnel tasked with preparing financial statements had no prior experience with preparing financial statements.

o The accounting systems used were not always able to generate accurate accounting information in the proper form to prepare the statements, so accounting personnel had to rely on manual methods, electronic spreadsheets, and estimates to prepare the statements.

o Final OMB guidance on form and content of the financial statements was not issued until after the end of the fiscal year.

o Management indecision during the year as to who was responsible for preparing the statements and at what reporting levels they should be prepared impeded planning for statement preparation.

OMB Bulletin No. 93-02 requires each agency to prepare, for each reporting entity under the CFO Act, an Overview of the Reporting Entity, Principal Statements, Combining Statements (if applicable), and Supplemental Financial and Management Information. The Notes to the Principal Statements are a required part of the Principal Statements. Section 3515 of the Act also requires each agency to submit its annual financial statement no later than March 31 of the following year. The Office of the DoD Comptroller did not provide the financial statements to the OMB until April 2, 1993. The statements were incomplete because they lacked the required Notes to the Principal Statements and the Supplemental Financial and Management Information. Those are integral parts of the financial statements necessary to fairly present the results of operations.

Debt Collection Act. Quarterly and annual reports to the Treasury on Accounts and Loans Receivable Due from the Public (Standard Form [SF] 220-9) were not accurately prepared. Quarterly reports were understated by about $60.0 million because the DFAS did not obtain feeder reports for all of the DBOF business areas. The annual report was overstated by $4.7 million due to a $29.5 million overstatement for the Defense agencies' and Navy business areas and a $24.8 million understatement for the Army and Air Force business areas. The errors in the annual report occurred because the DFAS did not reconcile the amounts reported to Treasury with the Accounts Receivable, Net

shown on the financial statements and because a $12.3 million error identified by the DFAS was not corrected before submission of the report to the Treasury. We also found that no systems were in place to manage the collection of debts from contractors.

The Debt Collection Act of 1982 (Public Law [P.L.] No. 97-365) expanded the rights given to Federal agencies by the Federal Claims Collection Act of 1966. The Debt Collection Act authorizes Federal agencies to assess interest, penalties, and administrative charges on debts owed by the public. The Debt Collection Act also authorized the Government to use such tools as credit bureaus and debt collection agencies and authorized the assessment of interest penalties and administrative costs against debtors with respect to debts owed to the United States. A debt is considered delinquent if it has not been paid by the date specified in the agency's initial demand letter, unless satisfactory payment arrangements have been made by that date, or if, at any time thereafter, the debtor fails to satisfy his obligations under the payment agreement. Once the penalty has been assessed and the appeal period has lapsed, interest, penalties, and administrative costs should be added to the penalty amount.

The SF 220-9, Report on Accounts and Loans Receivable Due From the Public, is required on an annual basis by the Treasury Financial Manual for all reporting entities, including those with no receivables. Entities with receivables of less than $50.0 million are required to submit annually, and entities having receivables of $50.0 million or more are required to report quarterly. The OMB Bulletin No. 93-02 requires that amounts shown as Accounts Receivable, Net-Non-Federal, agree with information on the SF 220-9 report. The DFAS is responsible for collecting debts and charging the prescribed interest, administrative fees, and penalties for the DBOF and preparing and submitting the required reports to the Treasury.

Quarterly Reports to Treasury. Managers for four of the five Air Force business areas did not submit the required feeder reports to the DFAS-Cleveland Center, Defense Accounting Office, Arlington, Virginia, needed to prepare the quarterly DBOF consolidated SF 220-9 Reports on Loans and Receivables Due from the Public. As a result, we estimated that quarterly reports for second and third quarters FY 1992 were understated by about $60.0 million. We were unable to review the feeder reports for the first quarter because the Defense Accounting Office had lost the reports. Responsible personnel at the DFAS-Denver Center did not submit the feeder reports because they had misunderstood the $50.0 million reporting threshold; they did not submit the required information because the business area's receivables were below $50.0 million. Because the Defense Accounting Office prepared a consolidated report and the $50.0 million threshold applied to the DBOF as a whole rather than the individual business areas, however, the consolidated quarterly reports were understated. Also, the Defense Accounting Office should have ensured that all business areas had been included in the consolidated reports before submitting the reports to the Treasury.

Also, SF 220-9 feeder reports for all five of the Air Force business areas did not report the collection of interest, penalties, or administrative costs. The trial

balances for those business areas did not indicate that such items were being collected as required by the Debt Collection Act.

Annual Reports to the Treasury. The amounts shown as Accounts Receivable, Net Non-Federal, on the financial statements for the DBOF did not agree with the amounts submitted to the Treasury on the SF 220-9, Report on Loans and Accounts Receivable Due from the Public for Fiscal Year 1992. This occurred because the two amounts had not been reconciled as required by OMB Bulletin No. 93-02. Table 1 shows the differences between the two amounts.

Table 1. Variances Between Accounts Receivable Due from the Public Shown on the DBOF Financial Statements and DBOF Accounts Receivable Reported to Treasury on SF 220-9 Annual Report

DoD Component	Financial Statements (Millions)	SF 220-9 Reports (Millions)	Statements Overstated (Millions)	Statements Understated (Millions)
Army	$ 7.6	$ 7.9	$ 0.0	$ .3
Navy	117.7	117.5	0.2	0.0
Air Force	93.0	117.5	0.0	24.5
Defense	125.8	96.5	29.3	0.0
DISA[1]	0.6	0.6	0.0	0.0
DeCA[2]	124.7	124.6	0.0	0.0
Total	$469.4	$464.6	$29.5	$24.8

1 Defense Information Systems Agency
2 Defense Commissary Agency

Contractor Debts. Contractor debts are currently being managed by the DFAS-Columbus Center. At the time of our audit, no system had been implemented to track debts from contractors. As a result, we could not determine whether such debts were being properly managed and reported. The DFAS-Denver Center is developing a system to manage contractor debt and expects to install the system during December 1993. We examined the documentation for the proposed system and it appeared to meet requirements of the Debt Collection Act.

Followup on Audit Report No. 92-021. Although the DFAS agreed to centralize management of DoD's debt collection function and to develop uniform operating procedures, such procedures had not been issued. Specifically, the DFAS agreed by the end of FY 1992 to:

o establish time frames for carrying out each procedure in the debt collection strategy,

o require collection activities to periodically report whether they meet the time frames,

o identify and write off all delinquent debts that are unlikely to be collected,

o require aggressive pursuit of all delinquent debts, and

o standardize the implementation of all procedures required by laws and regulations, including procedures for assessing interest, penalties, and administrative fees and for reporting uncollectible debts to the Internal Revenue Service.

As of the end of our field work, April 30, 1993, those uniform operating procedures had not been issued.

Improvements to Debt Collection. A standard debt collection system called the Defense Debt Management System has been developed by the DFAS-Denver Center and should be implemented at all DFAS Centers by July 30, 1993. The system features on-line processing, single-source data entry, automated interfaces from pay systems from which debts originate, and interfaces with other organizations. Documentation for the system showed that it will satisfy requirements of the Debt Collection Act. In addition, the DFAS has arranged for a centralized lockbox for its debt collections. A lockbox is a collection and processing service provided by a financial institution to accelerate the flow of funds to the Treasury's General Account. This service includes collecting the agency's mail from a specified post office box; sorting, totaling, and recording the payments; processing the items; making the deposit; and transferring the funds. Management told us that the lockbox had eliminated three personnel positions and the potential exists for eliminating more positions in the future.

DoD Accounting Manual. Air Force Supply Management-General Support Accounting Adjustments were not properly approved and documented; shipment discrepancies were not properly documented; interfund accounts payable transactions were not processed in the month they occurred; actual sales were not reported in financial statements; payments to contractors were not properly documented; consignments were not separately disclosed in financial statements; and accounting adjustments were not approved and documented as required by the DoD Manual 7220.9-M, "DoD Accounting Manual," as amended, June 17, 1991.

Department of Defense Appropriations Act, 1992, Section 8121. Policy managers for the DBOF did not take adequate steps to establish a separate subaccount for DBOF capital reserve funds as required by the Defense Appropriations Act. The DBOF's Capital Budget for FY 1992 was $1.2 billion. The DoD Comptroller issued capital asset guidance on July 21, 1992, that established new general ledger accounts to distinguish operating funds from capital asset funds. The guidance, however, was not issued until about 8 months after the law became effective; the new accounts have not yet been established by the business area managers; and it is questionable whether

the business areas can implement the guidance since only 1 of the 33 business areas is using the Standard General Ledger (see Part II, Internal Controls, Standard General Ledger). Additionally, we found the accuracy of the Monthly Report of Operations (DD Form 1307) used to track capital asset purchases questionable.

The DoD Appropriations Act, 1992, P.L. 102-172, Section 8121(d), effective November 26, 1991, required that a separate subaccount be established for recording and reporting all capital asset transactions. The subaccount would separate operating funds (funds used for all transactions that are not related to the acquisition of capital assets) from capital asset funds. A capital asset is a long-lived asset such as buildings, equipment, and improvements. Capital asset transactions are those that generate funds and recognize revenue from capital asset depreciation, as well as those that generate minor construction surcharges included in customer rates, obligations for capital asset purchases, and outlays for capital assets. The money for future capital asset investments is generated from depreciation and surcharges included in customer rates. A capital surcharge was applied by the DoD Comptroller for FY 1992 as a means of providing the initial seed money for future capital asset investments. This initial seed money totaled $1.3 billion.

Each fiscal year, each business activity's annual operating budget identifies the capital assets to be purchased during the year and the ceiling limitations for those assets. The business activities are permitted to purchase capital assets as long as they do not exceed their capital budget ceiling limitations. It was assumed by the business activities that since the capital assets were in their capital budgets, the money was available to be spent on capital investments. Therefore, operating funds were used, along with the money that was collected from depreciation and surcharges for capital assets, during the fiscal year.

The capital asset guidance was not issued in time to allow the business activities to properly account for capital asset transactions. The accounting systems used by the activities were not updated to include the new general ledger account codes; therefore, operating funds and capital money were not separately recorded. Until the capital reserve subaccount is established in the various accounting systems used by the DBOF or an alternate strategy to separate the fund is developed, the improper use of operating funds will continue.

The Monthly Report of Operations is a cumulative summary operating report used by the Office of the DoD Comptroller. Until early FY 1992, each DoD Component having one or more industrial fund activity groups was required to submit the Monthly Report of Operations, and DoD Components having one or more stock fund groups were required to submit the Monthly Management Report (DD Form 1302). Since December 1991, however, only the Monthly Report of Operations has been used to monitor operations within the DBOF.

The report is similar in design to that of an income statement, depicting revenues, expenses, and net results. Revenue is divided into three areas that identify the source of the activities' revenues: operations, surcharges, and other revenue. Expense is divided into six categories which, when totaled, equal the cost of sales. Net results, net operating results, and unfunded costs are also

parts of the report. In addition, two other items were added to the report to indicate the status of capital asset investments. Activities are to report the amount obligated for capital asset purchases for the year and net outlays for capital assets for the year to date. Chapter 95 of DoD Manual 7220.9-M provides guidance for preparing the Monthly Report of Operations.

Monthly Report of Operations. The required financial information for the Monthly Report of Operations was inconsistent, incomplete, and inaccurate. Guidance on the preparation of the report did not provide a crosswalk to the general ledger accounts. As a result, the DoD was unable to effectively track the true cost of operations or monitor the capital budget.

Prior to the establishment of the DBOF, guidance on the preparation of the report was provided in DoD Manual 7720.9-M. That guidance stated that the report is to be submitted within 45 days after the end of each month. If all financial data is not available at the required submission time, activities are to "provide the best estimate of any incomplete data and identify data as estimated." The guidance in DoD Manual 7220.9-M does not provide a crosswalk indicating the general ledger accounts that should be used in preparing the monthly report.

Headquarters, DFAS, issued a memorandum on October 11, 1991, which revised the content and format of the Monthly Report of Operations and required the report be submitted to the DFAS-Washington Center[1] 15 working days after the end of the month. However, this revision did not provide guidance on the preparation of the report, nor did it provide a crosswalk to the general ledger accounts to be used. Therefore, each of the DFAS Centers had to use its own designated accounts, cost codes and various methods to prepare the report. In addition, that revision did not address the issue concerning whether or not estimates should still be used if the financial data is incomplete. The financial data used to prepare the report is supposed to be taken from the same accounting systems that generate the trial balances used in preparing the year-end financial statements for each of the business activities. We performed a comparison of the Purchases of Property, Plant and Equipment shown on the FY 1992 financial statement of Cash Flows from Non-Operating Activities, with the Obligations and Net Outlays for capital equipment. Our comparison, shown in Table 2, identified significant differences between the two reports.

1 The DFAS-Washington Center was disestablished on September 30, 1992. The Monthly Report of Operations is currently being forwarded to DFAS-Cleveland Center, Defense Accounting Office, Arlington, VA.

Table 2. Comparison of the Statement of Cash Flows with Obligations and Net Outlays by Military Component and Defense Agency Business Area

Component	FY 1992 Financial Statements -- Statement of Cash Flows[2] (Millions)	Monthly Report of Operations -- Obligations and Net Outlays (Millions)	Difference (Millions)
Army	$ 519.1	$ 106.0	($ 413.1)
Navy	86.6	205.0	118.4
Air Force	3.2	403.0	399.8
DeCA	0.0	2.0	2.0
DISA	0.4	0.0	(0.4)
DLA	85.7	298.0	212.3
Totals	$ 695.0	$1,014.0	$ 319.0

2 These amounts were derived from line 17, "Purchases of Property, Plant, and Equipment," in the Cash Flows from Non-Operating Activities section of the Statement of Cash Flows.

Amounts on both financial documents should be equal if the same general ledger accounts are used for both. The Monthly Report of Operations is used by the DoD Comptroller to determine if each business area is operating within its operating and capital budgets. We question, therefore, whether the DoD Comptroller should authorize estimates to be used for the report.

At the present, personnel in the DoD Comptroller's Office agree that the financial information is not very reliable, especially the information received from the old stock fund business activities, since those business areas were not required to prepare the Monthly Report of Operations until the early part of FY 1992. As an extra precaution, the DoD Comptroller requires business area managers to verbally inform that office if it is anticipated that a business area is going to exceed its budget. In addition, Headquarters, DFAS, is revising the guidance on the preparation of the Monthly Report of Operations. That revised guidance will include a crosswalk indicating the general ledger accounts used for each line on the report. Until this guidance is issued, however, preparation of the monthly report will continue to follow the current guidance in DoD Manual 7220.9-M.

Federal Managers' Financial Integrity Act of 1982. The DeCA did not comply with FMFIA requirements. The DFAS and Air Force financial managers either did not accomplish FMFIA detail and general reviews in accordance with FMFIA or did not perform them adequately.

OMB Bulletin 93-02. The audit of Defense Business Operations Fund Depot Maintenance, Army (Army Audit Agency Project N2-471C) found that the DFAS did not follow DoD guidance on form and content of FY 1992

financial statements when classifying Army Depot Maintenance business area inventories.

The audit of the Fiscal Year 1992 Consolidating Financial Statements of the Department of the Navy's Defense Business Operations Fund (Project 93-0027) found that financial statements were inaccurate. For example, balances for Material-in-Transit and Progress Payments were not reported, financial records were adjusted to agree with the financial statements, negative balances in inventory records were not corrected and were included on the financial statements, and financial records for the Military Sealift Command did not accurately support and present accrual balances.

Real Property Ownership Under 10 U.S.C. § 2682, Facilities for Defense Agencies. Real properties, which by law are under the jurisdiction of the Military Departments, were improperly reflected as assets on the financial statements of the DBOF. Additionally, depreciation for real property is being improperly charged as an expense to the DBOF business areas and those expenses are being improperly charged back to the DBOF customers. Real property was included as an asset on the DBOF records because guidance issued by the Office of the DoD Comptroller on criteria for capitalization of assets required business area managers to include real property on their records. As a result, assets were overstated by $2.3 billion and depreciation expenses were overstated by about $135.0 million.

Section 2682 of title 10, U.S.C, Facilities for defense agencies, provides:

> The maintenance and repair of a real property facility for an activity or agency of the Department of Defense (other than a military department) financed from appropriations for military functions of the Department of Defense will be accomplished by or through a military department designated by the Secretary of Defense. A real property facility under the jurisdiction of the DoD which is used by an activity or agency of the DoD (other than a military department) shall be under the jurisdiction of a military department designated by the Secretary of Defense.

The DBOF was established under Section 8121(a) of P.L. 102-172, Department of Defense Appropriations Act, 1992. Section 8121(b) of P.L. 102-172 transferred to the DBOF "all assets and balances of working capital funds heretofore established...." The establishment of the DBOF, however, was subject to the provisions of 10 U.S.C. § 2208. The real properties under the jurisdiction of the Military Departments were not or are not assets of those working capital funds.

To implement Section 8121(b) of P.L. 102-172, the Office of the DoD Comptroller issued the "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992. The guidance states that ownership of capital assets used by the DBOF activities in providing goods or services must be recognized in the property and financial records of that business area. Additionally, the DoD Comptroller's guidance required the DBOF activities to charge a depreciation expense on their capital assets, including real property. Capital assets include, but are not limited to, property, plant, and equipment

items (including Government-owned facilities, property, and improvements to property acquired under a capital lease), equipment, and software. Real property includes land, buildings, and other facilities attached to the land.

Our review of the financial statements disclosed real property shown as assets of the DBOF. The real property assets used by the former Air Force and Army industrial and stock funds have been capitalized to the Component business areas of the DBOF. We could not determine, however, if real property used by the former Navy industrial and stock funds has been capitalized as DBOF assets because the financial statements were incomplete.

Furthermore, Section 8121(c) of P.L. 102-172 states that:

> Amounts charged for supplies and services provided by the Fund shall include capital asset charges which shall be calculated so that the total amount of the charges assessed during any fiscal year shall equal the total amount of (1) the cost of equipment purchased during that fiscal year ... and (2) the costs, **other than costs of military construction,** of capital improvements made for the purpose of providing services by the Fund [emphasis added].

We believe Section 8121 of P.L. 102-172 is consistent with 10 U.S.C. § 2682. If the DBOF managers wish to include the costs of real property in their results of operations, however, this can be accomplished through the use of rental agreements (interservice support agreements) with the DoD Component that has legal jurisdiction over the real property.

National Defense Authorization Act for Fiscal Years 1992 and 1993, Section 316. Section 316 of the Defense Authorization Act prohibits the addition of other functions, activities, funds, or accounts of the DoD to the Defense Business Operations Fund. During FY 1992, two new activities were added to the DBOF, the Defense Information Technology Services Organization (DITSO) and the Joint Logistics Systems Center (JLSC). We believe making these additions violated the prohibition. The DITSO was established to provide information technology services for the DoD Components within the DBOF. The JLSC was established to oversee the development of systems changes for the supply management and depot maintenance business activities of the DBOF.

The National Defense Authorization Act for FYs 1992 and 1993 authorized appropriations for those fiscal years for military activities of the DoD, military construction, and defense activities of the Department of Energy. Section 316 of the Act provides certain limitations on the use of the DBOF. One such limitation prohibits the addition to the DBOF of other functions, activities, funds, or accounts of the DoD.

Defense Information Technology Services Organization. On May 18, 1992, the DITSO was established as an activity governed by the Defense Information Services Agency. The mission of the DITSO is to design, engineer, develop, test, field, maintain, and operate information systems and networks for the business activities within the DoD. Those products and services are to be provided on a fee-for-service basis. The DITSO's FY 1992

customers included the DFAS Centers and selected portions of the Defense Logistics Agency. The DoD Comptroller provided a funding allocation of $1.8 million from the DBOF, enabling the DITSO to be established with no net increase in overall DoD resources.

Joint Logistics Systems Center. On February 11, 1992, the JLSC was chartered as a Corporate Management Center to facilitate the development of standard systems within the DoD, to manage systems development and integration, and to oversee the development of systems changes for the supply management and depot maintenance business activities of the DBOF. The JLSC will issue reimbursable orders to the Component's Central Design Activities to perform work on approved supply management and depot maintenance system support projects, which will be funded through the JLSC capital budget. The capital budgets of the Components were redistributed to the JLSC for management oversight purposes; therefore, the JLSC does not have any other funds, except those provided by the Components. The initial annual operating budget for the JLSC was established by transferring 80 percent of the capital budget approved for the Components' supply management and depot maintenance business activities. The Components will continue to request and justify their capital budgets with oversight and approval of the requests and related projects provided by the JLSC.

Prompt Payment Act. The Prompt Payment Act was enacted as P.L. 97-177 on May 21, 1982, and was amended on October 17, 1988, as P.L. 100-496. The Prompt Payment Act requires agencies to make payments on time, to pay interest penalties when payments are late, and to take discounts only when payments are made on or before the discount date.

Prior audits of The Prompt Payment Act identified that Finance and Accounting Offices were not complying with OMB Circular A-125, all early and late payments were not being reported, discounts were offered and not being taken, interest penalties were being incurred, interest was not being paid on late payments, and payments were issued without proper receiving reports. We identified that in FY 1992, the DFAS-Columbus Center was paying invoices late, payments were being paid after the due date, discounts were not being taken, interest penalties were being incurred, and interest was not being paid on late payments. The DFAS-Columbus Center reported 1.7 million invoices totaling $61.3 billion subject to prompt payment. Of those, 74,000 invoices valued at about $2.8 billion were reported by the DFAS as paid late. Interest on the late payments was reported at $8.9 million. In addition, we found that the Defense Commissary Agency did not comply with provisions of the Prompt Payment Act because it did not take advantage of offered discounts.

Instances of Noncompliance with DoD Accounting Policies. The DoD Memorandum, "Interim Stock Fund Policies," July 9, 1990, was implemented in FY 1991 and established the Cost of Operations Division (COD) that became part of the Air Force Supply Management business area of the Defense Business Operations Fund in FY 1992. The memorandum required the COD to account for all overhead costs incurred by Air Force Supply Management and Distribution Depots business areas. The costs include civilian and military personnel payroll expenses, travel, supplies, utilities, and depreciation. The

audit of Compliance with Laws and Regulations and Management Issues Related to Air Force Supply Management and Distribution Depot, FY 1992 Financial Statements (Project 93068001) found that Air Force did not properly identify and assign COD positions to permit the evaluation of actual costs associated with the management of inventory control point and distribution depot activities. We also found Air Logistics Centers did not compute reimbursements to the military pay appropriation as required by the DoD Memorandum, Interim Stock Fund Policies, July 9, 1990.

Our audit of Defense Finance and Accounting Service Revolving Fund Consolidating Financial Statements of the Defense Business Operations Fund for FY 1992 (Project 2FG-2004) found that the DFAS did not develop depreciation schedules for capital assets based on established useful life criteria. Also, assets had not been transferred in to the central design activities and information processing centers when capitalized, nor had assets been transferred out to the DITSO when it was established during FY 1992 as required by DoD Manual 7220.9-M and memorandum guidance from the DoD Comptroller, "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992.

We considered these material instances of noncompliance in forming our opinion on whether the Principal and Combining Statements are presented fairly, in all material respects, in conformity with the applicable accounting standards now in effect for the preparation of the entity's financial statements.

Except as described above, the results of our tests of compliance indicate that, with respect to the items tested, the managers of the DBOF complied, in all material respects, with the laws identified in Part IV, Appendix C, of this report, and with respect to items not tested, nothing came to our attention that caused us to believe that the management had not complied, in all material respects, with those provisions.

Management Comments

We received comments from the Acting Chief Financial Officer of the Department of Defense on June 17, 1993. Management disagreed that they had not complied with the Budget and Accounting Procedures Act of 1950 and Title 2. Management cited a section in OMB Bulletin No. 93-02 that states that executive agencies should continue using the applicable accounting standards now in effect for the preparation of the financial statements, pending adoption of Federal accounting standards by the principals of the Joint Financial Management Improvement Program.

Management indicated that financial statements had been provided to the OMB on April 1, 1993, not April 7, 1993, and DoD Component consolidating and business area financial statements were presented with the appropriate Notes and supplemental information.

Management agreed with our followup on Audit Report No. 92-021 and stated that a standard automated system called the Defense Debt Management System would be implemented in mid-1993.

Management did not agree with our discussion on the Monthly Report of Operations. Management believed that we referenced information that was 18 months out of date (i.e. the DoD Manual 7220.9-M) and misled the reader to believe that the DoD has not taken steps to correct known deficiencies.

Management disagreed with our reported noncompliance with OMB Bulletin No. 93-02. Management believed that the discussion on this issue was misleading because the Naval Audit Service reviewed only 4 out of 20 line items.

Management also disagreed that the addition of the DITSO and the JLSC to the DBOF violated the National Defense Authorization Act because the two new organizations did not represent new functions, activities, funds or accounts, but rather, were a reorganization of activities already within the DBOF.

The complete text of management's comments are in Part VI of this report.

Audit Evaluation of Management Comments

Until Title 2 and the Budget and Accounting Procedures Act of 1950 are repealed or rescinded, Federal agencies are still required to comply with them, even though OMB Bulletin No. 93-02 has reduced the level of emphasis on Title 2 as an accounting standard. Subsequent to OMB's release of OMB Bulletin No. 93-02, the Federal Accounting Standards Advisory Board recommended and the Joint Financial Management Improvement Program approved a hierarchy that constitutes an "other comprehensive basis of accounting" to be used for preparing Federal agency financial statements until a sufficiently comprehensive set of accounting standards are agreed to and published. Using this hierarchy, Title 2 should still be followed. Under OMB Bulletin No. 93-02, however, agencies no longer have to specifically show deviations from Title 2 in their financial statements.

We were told by OMB personnel that the OMB had received the DBOF financial statements on April 2, 1993; therefore, our final report was changed accordingly. On the DoD Component financial statements, Notes to the Consolidating Statements for the Navy portions of the statements, as well as the Supplemental Financial and Management Information for the Army and Navy portions of the financial statements, were also not included in the financial statements presented for audit.

Concerning management comments on our followup on Audit Report No. 92-021, our followup addresses the fact that uniform written procedures had not been issued as agreed. While a standard automated system for debt collection is a definite benefit, it, by itself, does not satisfy the intent of the recommendations for uniform operating procedures. Also, subsequent

discussion with management personnel in the Debt Collection branch of the DFAS-Denver Center indicated that estimated savings from use of the lockbox were overstated in the draft report. Accordingly, we have revised management's estimates of projected savings from the lockbox in this final report.

Although we were aware of the October 11, 1991, DFAS memorandum "Defense Business Operations Fund (DBOF) Reporting Requirements," which provided guidance on preparation of the Monthly Report of Operations, the memorandum did not address the problems identified in our report regarding a crosswalk to the general ledger. Nevertheless, we have revised our report to reflect this October 11, 1991, guidance.

Regarding compliance with OMB Bulletin No. 93-02, the Naval Audit Service audited specific line items from the financial statements. Those line items represent amounts that were material in relation to the financial statements. Line items audited totaled $25.2 billion, which is 80.6 percent of total assets and $7.8 billion of total liabilities for Navy DBOF. Also, those line items affected specific line items from the Statement of Operations (and Changes in Net Position); the Statement of Cash Flows (Indirect) or the Statement of Budget and Actual Expenses. For these reasons, we do not believe that our report is erroneous or misleading.

We continue to believe that the addition of the JLSC and the DITSO to the DBOF violated the prohibitions of section 316 of the Defense Authorization Act for Fiscal Years 1992 and 1993 which prohibits the addition of other functions, activities, funds, or accounts of the DoD to the DBOF. Both of these organizations were established in FY 1992 and added as DBOF business areas and were not specifically mentioned in P.L. 102-172 for inclusion in the DBOF.

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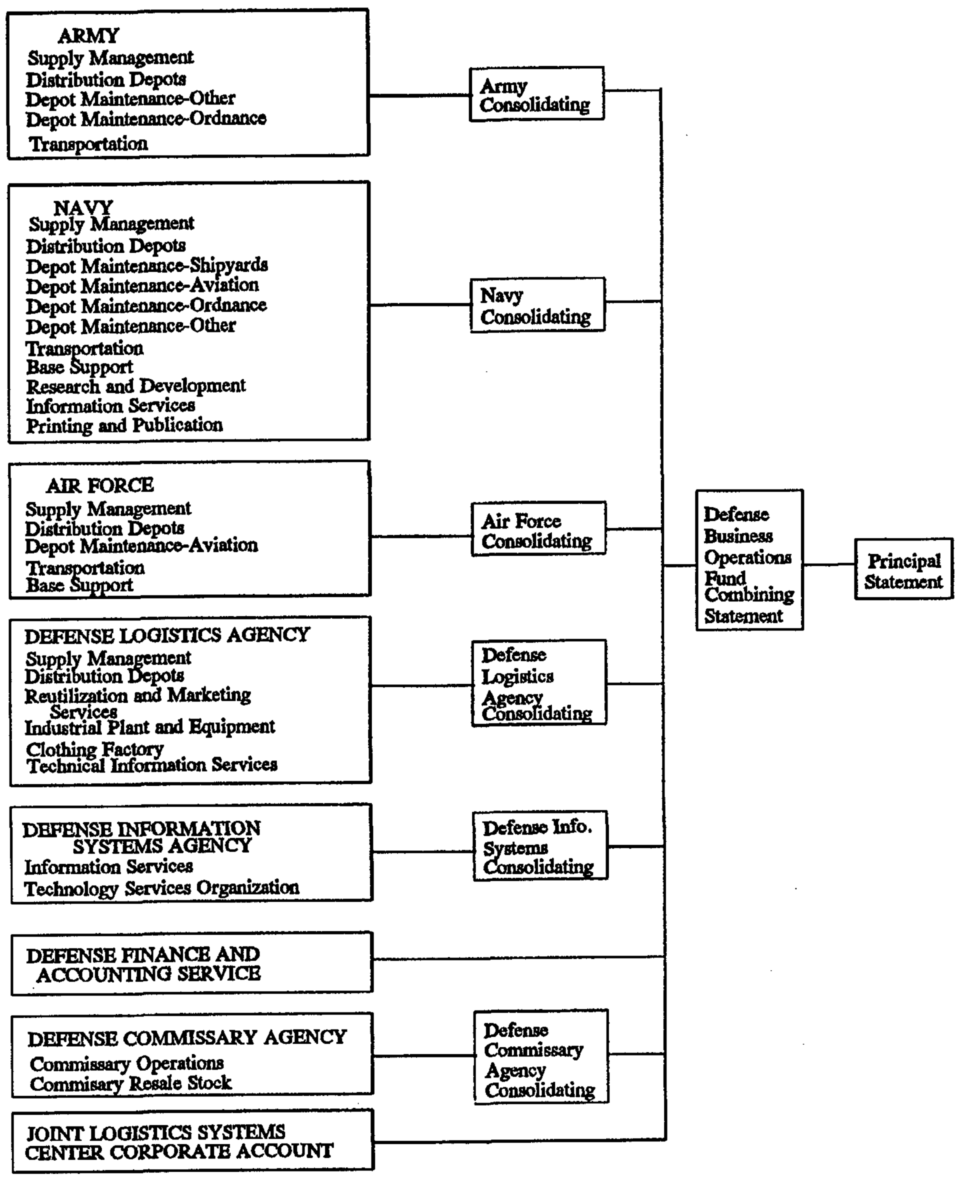
Part IV - Additional Information

Appendix A. Financial Statement Reporting Structure for the Defense Business Operations Fund



Appendix B. Summary of Audit Work Performed by Others

Component	Business Area	FY 1992 Reported Assets	FY 1992 Reported Expenditures	Audit Work Performed by	Scope of Audit Work Performed	Audit Project Number
Army	Supply Management	$17.168,076.716	$26,127.306.745		None	Unaudited
	Distribution Depots	0	182.998,398		None	Unaudited
	Depot Maintenance-Other	1.903,201.359	2.004.236.013	Army Audit Agency	Full	N2-471C
	Depot Maintenance-Ordnance	715,642.948	689.348.467	Army Audit Agency	Full	N2-471C
	Transportation	251,726.071	477.990.318	Army Audit Agency	Full	N2-473C
Navy	Supply Management	20,398,996.514	20.979.562,426	Naval Audit Service	Limited [1]	92-0104
	Distribution Depot	(33.966.845)	401.037,304		None	Unaudited
	Depot Maintenance-Shipyards	2,354.383.710	5.428.536,303	Naval Audit Service	Limited [1]	92-0163
	Depot Maintenance-Aviation	1,240.656.653	3.097.477,056	Naval Audit Service	Limited [1]	92-0163
	Depot Maintenance-Ordnance	512,173.909	877,458,677	Naval Audit Service	Limited [1]	92-0163
	Depot Maintenance-Other	101.455.618	181.167.810	Naval Audit Service	Limited [1]	92-0163
	Transportation	2,289.358.046	2.920.960,716	Naval Audit Service	Limited [1]	92-0155
	Base Support	894.986.026	1.492.750,468	Naval Audit Service	Limited [1]	92-0099
	Research and Development	3,177.797,520	6.216.759.154	Naval Audit Service	Limited [1]	92-0149
	Information Services	79.484,921	287.226.196		None	Unaudited
	Printing	205.595.331	284.972.014		None	Unaudited
	Navy Consolidated					N/A
Air Force	Supply Management - Fuels	41.339.949.430	19,361.780.017	Air Force Audit Agency	Full	92068011
	General Support					92068010
	Cost of Operation					92068004
	Repairable Support					92068012
	Systems Support					92068040
	Distribution Depots	(40.825,014)	64.550.568	Air Force Audit Agency	Full	93068012
	Depot Maintenance-Aviation	3,075.272.016	3.571.476.178	Air Force Audit Agency	Full	92068002
	Transportation	800.204.712	3.139.421,437	Air Force Audit Agency	Full	92071002
	Base Support	6.989,475	7.039,411	Air Force Audit Agency	Full	92068003

1 The audit was limited to a review of the following financial statement line items - Financial Resources: Inventory Held for Sale, Net; Non-Financial Resources: Inventories Not Held for Sale: and Non-Financial Resources: Property. Plant and Equipment. Net.

Appendix B. Summary of Audit Work Performed by Others

Component [2]	Business Area	FY 1992 Reported Assets	FY 1992 Reported Expenditures	Audit Work Performed by	Scope of Audit Work Performed	Audit Project Number
Defense Logistics Agency	Supply Management	13,324.389,086	12.325,462.870	DoD Inspector General	Limited [3]	2LD-5020
	Distribution Depots	(53,475,033)	1.159,287.555		None	Unaudited
	Reutilization and Mkting Svcs	139.536.513	280,171.628		None	Unaudited
	Industrial Plant and Equip Ctr	(3.662,477)	39,060,392		None	Unaudited
	Clothing Factory	6,487.901	34,515.771		None	Unaudited
	Technical Info Services	34,935.252	11.923,551		None	Unaudited
DISA	Information Services	395,340.667	1.230.831.970	DoD Inspector General	Full	1FH-2001
	Info Tech Svcs Org Info Svcs	190,142.366	60.786,187		None	Unaudited
DFAS	DFAS Operations	280,187.603	536.738.562	DoD Inspector General	Full	2FG-2004
DeCA	Commissary Operations	(806,594.206)	1.027.281.818		None	Unaudited
	Commissary Resale Stocks	1.724.584,770	6.029,756.316	DoD Inspector General	Full	1FE-1003
JLSC	Joint Logistics System Center	9.744.417	7.295.628		None	Unaudited
Total		$111.682.775.975 [4]	$120.537.167.924 [4]			

2 DISA = Defense Information Services Agency; DFAS = Defense Finance and Accounting Service: DeCA = Defense Commissary Agency; JLSC = Joint Logistics Service Center

3 The audit was limited to a review of Ground Fuels.

4 Total assets and total expenditures do not agree with the Principal Statement due to the exclusion of the Departmental total and mathematical errors in the DBOF financial statements.

Appendix C. Laws and Regulations Reviewed

Antideficiency Act, Public Law (P.L.) 93-344, February 27, 1906

Budget and Accounting Procedures Act of 1950, September 12, 1950

Military Construction Codification Act, P.L. 97-214; 10 U.S.C. § 2682, July 12, 1982

Federal Managers' Financial Integrity Act of 1982, P.L. 97-255, August 19, 1982

Debt Collection Act, P.L. 97-365, October 25, 1982

Prompt Payment Act of 1988, P.L. 100-496, October 17, 1988

Chief Financial Officers Act of 1990, P.L. 101-576, November 15, 1990

Department of Defense Appropriations Act, 1992, P.L. 102-172, Section 8121, November 26, 1991

National Defense Authorization Act for Fiscal Years 1992 and 1993, P.L. 102-190, Section 316, December 13, 1991, as amended by the National Defense Authorization Act for Fiscal Year 1993, P.L. 102-484, Section 341, October 2, 1992

Joint Financial Management Improvement Program Core Financial System Requirements (FFMSR-1, January 1988)

Treasury Financial Manual, June 12, 1990

U.S. Standard General Ledger, November 12, 1992

General Accounting Office's "Policy and Procedures Manual for Guidance of Federal Agencies," Title 2, "Accounting," May 18, 1988

OMB Bulletin 93-02, "Form and Content of Agency Financial Statements," October 22, 1992

DoD 7220.9-M, "DoD Accounting Manual," as amended, June 17, 1991

"DoD Guidance on Form and Content of Financial Statements for FY 1992 Financial Activity," December 30, 1992

Appendix D. Organizations Visited or Contacted[1]

Office of the Secretary of Defense

Office of the Comptroller of the Department of Defense, Arlington, VA

Department of the Navy

Headquarters, U.S. Marine Corps, Arlington, VA
Office of the Comptroller, Department of the Navy, Washington, DC

Defense Agencies

Headquarters, Defense Finance and Accounting Service, Arlington, VA
- Defense Finance and Accounting Service Center, Cleveland, OH
  - Defense Accounting Office, Cleveland Center, Pensacola, FL[2]
  - Defense Accounting Office, Cleveland Center, Arlington, VA[3]
- Defense Finance and Accounting Service Center, Columbus, OH
- Defense Finance and Accounting Service Center, Denver, CO
- Defense Finance and Accounting Service Center, Indianapolis, IN

U.S. Transportation Command, Scott Air Force Base, Belleville, IL
Defense Information Systems Agency, Arlington, VA
- Defense Information Technology Service Organization, Denver, CO
- Defense Information Technology Service Organization, Columbus, OH

Defense Logistics Agency, Alexandria, VA

Non-Defense Federal Organizations

Department of the Treasury, Washington, DC
Office of Management and Budget, Washington, DC
General Accounting Office, Washington, DC
Federal Accounting Standards Advisory Board, Washington, DC

1 Organizations visited or contacted by the Service's audit organizations are not included in this Appendix.
2 Formerly the Financial Information Processing Center, Naval Education and Training Program Management Support Activity.
3 Formerly the Naval Regional Finance Center, Navy Accounting and Finance Center.

Appendix E. Report Distribution

Office of the Secretary of Defense

Assistant Secretary of Defense (Public Affairs)
Comptroller and Chief Financial Officer of the Department of Defense
Deputy Chief Financial Officer of the Department of Defense

Department of the Army

Secretary of the Army
Assistant Secretary of the Army (Research, Development and Acquisition)
Inspector General, Department of the Army
Auditor General, Army Audit Agency

Department of the Navy

Secretary of the Navy
Commandant of the Marine Corps
Assistant Secretary of the Navy (Financial Management)
Comptroller of the Navy
Auditor General, Naval Audit Service

Department of the Air Force

Secretary of the Air Force
Assistant Secretary of the Air Force (Acquisition)
Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, Air Force Audit Agency

Defense Agencies

Defense Finance and Accounting Service
- Defense Finance and Accounting Service-Cleveland Center
  - Defense Accounting Office, Pensacola, FL
  - Defense Accounting Office, Arlington, VA
- Defense Finance and Accounting Service-Columbus Center
- Defense Finance and Accounting Service-Denver Center
- Defense Finance and Accounting Service-Indianapolis Center

U.S. Transportation Command
Defense Information Systems Agency
- Defense Information Technology Service Organization

Defense Logistics Agency

Non-Defense Federal Organizations

Department of the Treasury
Office of Management and Budget
U.S. General Accounting Office
- Accounting and Financial Management Division
- National Security and International Affairs Division Technical Information Center

Federal Accounting Standards Advisory Board
Joint Financial Management Improvement Program

Chairman and Ranking Minority Member of Each of the Following Congressional Committees and Subcommittees:

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on Defense, Committee on Appropriations
House Committee on Armed Services
House Committee on Government Operations
House Subcommittee on Legislation and National Security, Committee on Government Operations

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Part V - Principal and Combining Financial Statements of the Defense Business Operations Fund - FY 1992

OFFICE OF THE COMPTROLLER OF THE DEPARTMENT OF DEFENSE

WASHINGTON DC 20301-1100

APR 1 1993

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING, DOD

SUBJECT: Transmittal of Defense Business Operations Fund Financial Statements on FY 1992 Financial Activity

Attached are Financial Statements for the Defense Business Operations Fund (Fund) on FY 1992 financial activity. These statements are submitted for audit as required by the Chief Financial Officers Act of 1990. The Fund's annual financial statements include the following DoD Component reporting entity and Consolidating reports:

- Defense Business Operations Fund Principal Statements
- Defense Business Operations Fund Combining Statements
- Army Defense Business Operations Fund
- Navy Defense Business Operations Fund
- Air Force Defense Business Operations Fund
- Defense Logistics Agency Defense Business Operations Fund
- Defense Information Systems Agency Defense Business Operations Fund
- Defense Finance and Accounting Service Defense Business Operations Fund
- Defense Commissary Agency Defense Business Operations Fund
- Joint Logistics Systems Center Defense Business Operations Fund.

The financial statements do not include "Notes to the Principal Statements" for the Fund's Principal Statements and "Notes to the Consolidating Statements" for the Navy portions of the statements; or the "Supplemental Financial and Management Information" for the Army and Navy portions of the financial statements. Those sections are expected to be transmitted to your office by mid-April, 1993.

My staff, and those of the DoD Components are available to provide assistance and information that you may require in the upcoming audit of these financial statements. This office will work with your staff to make those adjustments and improvements necessary to ensure the financial statements present fairly, in all material respects, the assets, liabilities, and net financial position, of the Defense Business Operations Fund as of September 30, 1992.

Alvin Tucker
Acting Chief Financial Officer

Attachment

OVERVIEW TO THE DEFENSE BUSINESS OPERATIONS FUND

DEFENSE BUSINESS OPERATIONS FUND OVERVIEW

I. BACKGROUND

A. Establishment of the Defense Business Operations Fund

The Department of Defense expanded the use of businesslike financial management practices through the establishment of the Defense Business Operations Fund (Fund) on October 1, 1991. The Fund operates with financial principles that provide improved cost visibility and accountability to enhance business management and improve the decision making process. The Fund builds on revolving fund principles previously used for industrial and commercial-type activities. Successful implementation of the Fund is essential to achievement of the following initiatives: (1) consolidating like functions, (2) increasing cost visibility, and (3) realizing significant monetary savings through better business practices.

Revolving funds were originally established to satisfy recurring Department of Defense requirements using a businesslike buyer-and-seller approach in their operation. The generators of requirements justify the need for funds to the Congress, but are not always the organizations that execute the requirement. In some instances, the "requirers" or "customers" contract with the DoD organizations, the "providers" or "sellers," who have expertise in the service or product required. The customers and providers operate under business-type financial management principles. Revolving funds provide the best financial structure for businesslike operations.

The establishment of the Fund does not change any previous organizational reporting structure or command authority relationship. Combining business activities under a single treasury code allows consolidation of cash management, while functional and cost management responsibilities remain with the Military Departments and Defense Agencies.

B. Evolution of Revolving Funds

Revolving funds have been in use by the military for a considerable period of time. In fact, the Navy had a revolving fund as early as 1878. Modern day revolving fund authority is provided by the National Security Act of 1947, as amended (Title 10 U.S.C. Section 2208) which allows the Secretary of Defense to establish revolving funds as a means of more effectively controlling the cost of the work performed by DoD.

Revolving fund activities as established in the 1950's and 1960's have evolved into two distinct categories. The first category (stock funds) dealt with procuring materiel in volume from commercial sources and holding it in inventory. Subsequently, the fund sold this materiel to the Military Service

customer in order to achieve weapon systems readiness and provide required personnel support items. The second category (industrial funds) served activities that provided industrial and commercial goods and services such as depot maintenance, transportation, and research and development. Both types of revolving funds were financed primarily by reimbursements from customers' appropriated funds.

Beginning in FY 1991, the distinction between the two categories of funds began to disappear with the addition of operating costs to the stock funds. One of the major distinctions between stock and industrial funds before FY 1991 had been the charging for overhead operations costs, as the industrial funds procedures included recovery of these costs. This change to stock funds was made in recognition of the fact that the selling prices to customers of both categories of revolving funds should include all the costs of providing materiel or industrial goods and service. By identifying all of the costs of providing a service, and giving the manager the authority and flexibility to make trade-off decisions, more can be done to control costs and promote efficiencies. Without identification of all applicable costs, the ability of a manager to control costs and promote efficiencies are unnecessarily limited.

II. OPERATIONAL OVERVIEW

A. Purpose

The primary goal of implementing the Fund is to provide a business management structure that encourages managers and employees of DoD support organizations to provide quality products or services at the lowest cost. A major feature of this business management structure is increased emphasis on business operations. This business operations structure identifies each business area, the products or services, and the total cost of operations within that business area.

Under this structure, customers establish requirements and are charged, through the rate structure, for the cost of industrial and commerical-type services and products provided. Providers, in turn, produce quality goods and services which satisfy customer requirements at the lowest cost. In other words, support organizations incur costs based on customer orders. This linkage of support costs to customer funding ensures better communication between the customer and the provider. By making the producing organization responsible for managing all costs associated with delivering the goods or services, those managers will identify cost drivers and can focus their management improvement efforts accordingly. Better cost visibility enables managers at all levels to make informed decisions.

Applying the concept of managing to total cost provides increased flexibility to both customers and providers. Customers have the visibility of the true costs of their support requirements, so that effective trade-off decisions can be made on the level of support service they require as they assess operational demands. Providers, on the other hand, have the visibility of their total costs in satisfying customer requirements, so that processes used in producing the goods or providing the services can be evaluated and improvements and efficiencies implemented.

The Fund also provides the framework for evaluating investment requirements in terms of operational costs. For example, if a manager can determine that an investment will help achieve long-term lower costs, there is more of an incentive to make that investment. All capital investments are depreciated and those depreciation costs then become part of the operating cost of providing a product. Benefits accrue to the business and savings are realized when payback is achieved faster than the depreciation schedule. Reduced production costs for the provider translate to reduced prices for the customer, thereby enabling the Department to more effectively accomplish its mission within available resources.

The Fund achieves the desired result of expanding the relationship between the customer (normally the operating forces) and the provider (the support establishment). The Fund expands the availability of business management information and provides a structure that supports the customer-provider relationship. The focus is on quality customer service at reduced costs.

B. Vision

A significant segment of the Department provides goods and services similar to those provided in the general economy. It has been demonstrated throughout history that a "market economy" provides the most effective method of apportioning resources among competing requirements. The underlying concept of the Fund is that procedures developed by private corporations operating in the general economy can be applied to the support establishment. With the establishment of a market based economic system in the support establishment, both the provider and the recipient or customer of goods and services will be made to focus on the most efficient method of accomplishing assigned missions.

To provide the business areas of the Department the tools to increase their effectiveness and efficiency, a number of initiatives are underway. These initiatives include the consolidation of accounting and financial services and the development of standard systems through the Business Information Management effort. Within these initiatives, there will be standard cost systems; integrated systems that will ensure the consistency of information and therefore the usefulness, timeliness, and accuracy of information available to managers at all levels; and financial systems that comply with the Chief

Financial Officers Act and other guidance on accounting principles and standards. These initiatives will ensure that the same information will be available for costing, management, and budgeting, including improved valuation and information on inventory, labor costs, overhead costs, capital, and revenue. Under way is the development of new inventory valuation policies and methods. Currently inventory held for sale is valued at the latest acquisition price in lieu of a stabilized price. Inventory identified as excess is valued at 3% of the acquisition cost which is the average return realized by the sale of surplus property. Inventory items in need of repair are valued at the acquisition cost less the cost of repair. Revisions to these methods are being considered, to take into account changes in acquisition costs, returns, and the impact of holding cost on the inventory valuation. These changes are being discussed with the General Accounting Office, Federal Accounting Standards Advisory Board, and supply managers in DoD. The final methodology will be incorporated in functional requirements developed for logistics and financial systems modernization and development. And finally, there will be an integration of quality and performance reporting and goals into the financial management system.

The decision to consolidate many of the Department's business areas into a single fund requires more than just a change in mechanics. The full value of the initiative will not be realized without a change in the corporate mind-set. In these competitive times, it is essential that new approaches be explored and incorporated into daily management practices.

The Fund provides better visibility, at every level of management, of the total cost of operating support activities. Customers of the Fund (activities that create demand for support services) are made aware of the economic consequences of their requirements because these costs are included as part of their (i.e., customer) budgets. Budget reviewers and other managers, both within and outside the Fund, also have improved visibility because they can look to the financial system to see the total cost of required support services. The budget review process can better consider work load forecasts from the perspective of force structure and operating tempo changes; it can review assumptions about productivity improvement rates; and it can ensure that strategies to achieve productivity improvements are planned and resourced in the budget formulation process. In the past, it was difficult for budget reviewers and other managers to identify the total cost of support activities because these costs were distributed across several different accounts in the budget, each justified independently from the others.

The business relationship between providers and customers fully supports the Department's move toward total quality management. Unit cost resourcing and Business Operations Fund management provides a meaningful tool to focus and reinforce the effectiveness of such management improvement strategies as total quality management. Unit cost not only provides managers total cost per output, but also allows identification of the processes

that increase total cost which improves the manager's ability to control cost drivers. It provides a framework for involving the work force to improve the quality of processes, eliminating costly rework and delays which, in turn, lower cost per output at a given level of performance. Productivity gains can be achieved through quality improvements. Unit cost data, in combination with performance measures, provides the ability to assess the effectiveness of process improvement initiatives and also provides a basis for gain sharing and other organizational incentives. Customer-provider relationships ensure that level of performance is what the customer is willing to buy at a given price.

C. <u>Concept of Operations</u>

The Fund combines existing commercial or business operations that were previously managed as individual revolving funds into a single revolving, or business operations, fund. Besides the prior industrial and stock fund businesses, some activities which were not previously financed on a revolving fund basis are included as business areas in the Fund. Examples include finance and accounting services, reutilization and marketing services, industrial plant equipment maintenance and repair, and technical information services. The visibility of total costs related to operational mission requirements is improved because a more comprehensive range of support services is included in the budgets and costs of the operational forces requiring these services.

The establishment of the Fund does not change any previous organizational reporting structure or command authority relationship. Combining business activities under a single treasury code allows consolidation of cash management, while functional and cost management responsibilities remain with the Military Departments and Defense Agencies. Prices for goods and services produced in a Component's business area remain the responsibility of that Component and are set on a break-even basis over the long term at the business area level. Profits, when they occur, are returned to customers through lower rates in subsequent years, while possible losses are recouped through increased rates in subsequent years.

The Fund's financial procedures provide increased flexibility to enhance management discretion. The annual budget documents for each business in the Fund provide clear guidance as to the Department's expectation of financial performance. Each business area receives both an operating and a capital budget. During FY 1992, a major effort has taken place in each business area to improve the delineation between capital investments and operating costs. This delineation provides better visibility and more meaningful identification of operations costs to all levels and identifies total cost of the business area. Where feasible, unit cost goals are provided for each output identified within each business area. In some instances, the nature of the outputs do not lend themselves to unit measurement. In those

instances, an overall financial goal for that output is established.

While the changes necessary to improve information are in the formative stages, some specific improvements to enhance the visibility of costs for the businesses previously managed under industrial and stock funds will be implemented. Base operations support and headquarters costs, which were often excluded from revolving funds, will be included as part of the operating cost of the business areas in the Fund. Depreciation of capital investments will be included to reflect the impact of investment decisions in the prices and unit cost goals of the business areas.

No other dollar or personnel restrictions accompany the operating budgets for the businesses in the Fund. Overall resource utilization is ultimately determined by the level of outputs produced. The business manager is expected to keep costs within the sum of approved cost goals times the customer determined work load. This management concept provides the manager the opportunity to make trade-off decisions for the best operating results within the business area. In the past, restrictions or limitations on trade-offs between elements of cost within a business operation may have driven managers to less efficient decisions, ultimately increasing the total cost of the business. While the DoD Comptroller is working to minimize restrictions, the operating budgets do not supersede other policy decisions or legislative limitations.

D. Scope of the Fund

The Fund consists of business areas that were previously managed using industrial or stock funds and a few additional Defense Agency activities that also lend themselves to a business management mechanism. Business areas included in the Fund are:

Supply Management (A, N, AF, DA)
Distribution Depots (A, N, AF, DA)
Depot Maintenance (A, N, AF)
Base Support (N, AF)
Transportation (A, N, AF)
Research and Development Activities (N)
Printing and Publication Services (N)
Information Services (N, DA)
Defense Commissary Agency (DA)
Defense Clothing Factory (DA)
Defense Finance and Accounting Service (DA)
Defense Technical Information Center (DA)
Defense Reutilization and Marketing Service (DA)
Defense Industrial Plant Equipment Center (DA)

(Legend: "A" = Army; "N" = Navy; "AF" = Air Force; "DA" = Defense Agency)

Some business areas included are exclusive to just one component (i.e., Military Service or Defense Agency) even though other Components perform the same functions. This is because some Components had previously categorized a support activity as an industrial fund operation, while others had not. The Department will review these areas to determine whether all Component activities in these business areas should be included in, or excluded from, the Fund. The Department will continue to review the appropriateness of expanding some activities in the Fund and adding new support activities in the future. However, pursuant to commitments to the congressional committees and the General Accounting Office (GAO), no additional businesses were added in FY 1992 or will be added in 1993.

Business Area Descriptions

1. Supply Management. The Supply Management business area includes inventory management of approximately five million items, including weapon systems spare parts, food, clothing, fuel and medical supplies. The business area encompasses the various inventory control points in the Army, Navy, Air Force and Defense Logistics Agency. Each DoD Component in the business area procures materiel for its customers and makes repair parts available in support of military readiness. Materiel is procured from contractors and held in inventory for sale to authorized customers. Customers purchase the materiel using appropriated funds, primarily Operations and Maintenance. Prices for items purchased cover the acquisition cost plus the cost of supply operations and transportation. Actions are underway to refine Department pricing practices to more discretely identify the costs included in surcharges to customers. We are developing pricing mechanisms that accurately align cost and price to allow differing levels of service. This structure would provide greater flexibility to customers and providers. Plans call for re-evaluation of the business area output measure to determine if another measure will more accurately reflect work load volume.

2. Distribution Depots. The Distribution Depot business area includes all the DoD general supply distribution depots. It includes the functions related to receiving, storing and shipping the items purchased by supply management materiel managers in the Army, Navy, Air Force and Defense Logistics Agency (DLA). The Department is consolidating the distribution depots under DLA and has a continuing effort related to migrating unit cost reporting for depots from the Military Services to DLA as the depots transfer. Unit cost policies require that receipts and issues at depots be identified to the inventory control points (ICP) who manage the items and direct those receipts and issues. A matrix of depot to ICP work load is key to effective unit cost execution. An effort is underway to develop the matrix from individual transactions and provide the matrix on a monthly basis. The matrix will become the basis of costing between depots and ICPs for the integrated aspect of these business areas.

3. Depot Maintenance. This business area encompasses maintenance, repair and manufacturing activities of the three Services such as shipyards, ordnance plants, aircraft maintenance facilities, and tank and automotive maintenance facilities. Activities included in the Depot Maintenance business area were formerly identified in the Service industrial funds. Direct costs are collected by individual job and completed jobs are billed to customers based on the quantity of direct labor and materiels consumed as well as the appropriate share of allocated indirect and general and administrative costs. Long-term plans call for the development of catalogs containing fixed prices for the various types of jobs these activities perform. In addition, unit cost reports will be developed to complement the catalogs. These management information reports will be used to monitor execution against unit cost budgets and provide information on cost and output performance.

4. Base Support. The Base Support business area is comprised of Naval Facilities Engineering Command Public Works Centers (PWCs), the Naval Academy Laundry, and the Air Force Laundry and Dry Cleaning Service. The Navy has several PWCs across the country and overseas that provide facility maintenance, utility services, and other engineering support services to the installation and its tenant activities. Customers are billed for the direct costs of repair and maintenance and an allocated share of indirect and general and administrative costs. Utilities and sanitation services are sold based on usage. The Naval Academy laundry and the seven Air Force laundry and dry cleaning plants provide service to authorized activities and individuals at costs competitive with commercial facilities. Direct costs are collected by individual job and completed jobs are billed to customers based on the quantity of direct labor and materiel consumed as well as the appropriate share of allocated indirect and general and administrative costs. Action is underway to review comparable functions in the Components for adoption of customer-provider relationships.

5. Transportation. Included in this business area are the three transportation commands--the Military Traffic Management Command, the Military Sealift Command, and the Air Mobility Command. These organizations were formerly included in the Military Service industrial funds. These commands accumulate and distribute costs to outputs measured primarily in terms of cargo movement (e.g., measurement tons). Unit cost reports are being developed to improve the financial and budget information available for these activities.

6. Research and Development. The Research and Development (R&D) business area is now limited to Navy research activities. Navy R&D functions were the only industrially funded research activities within the Department when the Fund was established. There are multiple centers and labs throughout the United States. The Navy centers provide research and development, engineering, and test and evaluation support for weapons system programs.

Direct and overhead costs are collected by job and billed to customers. Near-term plans call for the development of unit cost reports and financial reports for the Navy activities currently in the Fund. Actions underway include studying the feasibility of adopting this business relationship in R&D functions of other Services and Agencies.

7. Printing and Publications. Publishing and Printing Services involve the management and operation of a worldwide printing production and procurement network. Effective with FY 1992, the Navy Publishing and Printing Service has been designated as the single manager for DoD printing.

8. Information Services. The Information Services business area contains the Defense Information Services Agency and the Naval Computer and Telecommunications Station of the Naval Computer and Telecommunications Command. The business area provides communications services to DoD and other Federal Agencies, in addition to system design development and automated data processing support for the Navy. The activities in this business area were previously identified and funded in the industrial fund, and therefore were operating on a fee-for-service basis. Unit cost reports are currently being developed to improve the financial and budget information available for these activities. Long-term plans call for the development of unit cost reports for central design activities and data processing installations that are currently funded outside the Fund.

9. Commissary Operations. The Defense Commissary Agency operates DoD commissaries worldwide and provides troop issue subsistence for the Air Force and the Army at selected locations. Commissaries provide products at the lowest practical price (consistent with quality) to members of the Military Services, their families, and other authorized patrons, while maintaining high standards for quality, facilities, products, and services. Commissary operations are not funded through customer orders, rather through direct appropriation to the Fund. Unit cost reports are presently under development to support financial management in this business area.

Commissary Resale Stock. The commissary resale business area finances the inventory of commissary goods sold to commissary customers through revolving fund operations under the Fund. This business area procures commissary inventory to sell to authorized commissary patrons (active duty military, retired military, reservists who perform active duty, and certain diplomatic service personnel and their families). Income from the sale of the inventory is reinvested in inventory to support the commissary sales. Unit cost reports are presently under development to support financial management in this business area.

10. Clothing Factory. The Clothing Factory manufactures clothing and textile items for all DoD Components. Items typically manufactured are those which may be required on short notice, in small lots, with special measurement, or under other conditions which make procurement from commercial sources infeasible. Direct costs are collected by individual job and completed jobs are billed to customers based on the quantity of direct labor and materiels consumed as well as the appropriate share of allocated indirect and general and administrative costs.

11. Financial Operations. This business area encompasses the Defense Finance and Accounting Service (DFAS) headquarters and five finance centers which provide a full spectrum of finance and accounting services, such as civilian and military payroll, contractor payments and departmental level accounting. DFAS was created on January 15, 1991, through the consolidation of the primary finance and accounting centers of the Military Departments and Defense Agencies. Financial management for the DFAS is supported by a unit cost resourcing system where costs are aligned with the products and services produced. Reports are generated at the activity level and summarized to the business area. Under Defense Management Report Decision 910, approved on December 13, 1991, all Component installation and intermediate command finance and accounting activities will transfer to DFAS and be incorporated into the financial operations business area. Our plans call for the expansion of the current unit cost and financial reporting systems to include these consolidated activities.

12. Technical Information Services. The Technical Information Services business area is comprised of the Defense Technical Information Center (DTIC) and the 14 DTIC administered Information Analysis Centers. DTIC functions as the central collection and dissemination point for the DoD technology base information. Customers in FY 1992 include the Service and Defense Agency Research, Development, Test and Evaluation account managers that sponsor registered users who have access to the technical information services data bases. This will be refined in FY 1993 as a catalog of prices will be developed to bill individual customers requesting data for the cost of specific outputs. In addition, unit cost reports are currently being refined for DTIC.

13. Defense Reutilization and Marketing Service (DRMS). The reuse of excess and surplus property within the government and other authorized agencies and the sale of the remaining property is the primary mission of this business area under DLA. Reutilization can result in cost avoidances by reducing unnecessary procurements. Items not reutilized within DoD are screened for possible transfer to other Federal agencies or for donation to local governments. DRMS also has the mission of hazardous property disposition. In this capacity, they handle the vast majority of DoD property governed by the Resource Conservation Recovery Act (RCRA of 1976 as amended. Unit cost reports are being refined to s.:: rt financial management in this

business area. Also under development is a fee structure to recover the costs of the reutilization mission.

14. Industrial Plant Equipment. The Defense Industrial Plant Equipment Center, a field activity of the DLA, repairs current in-use industrial plant equipment (IPE). The Defense Industrial Reserve Act provides for an industrial reserve of machine tools. Since FY 1987, amendments to this act require the Services to pay for the repair, overhead, and storage of IPE transferred from the General Reserve. For the IPE business area, a catalog of fixed prices is under development similar to that for depot maintenance. In addition, unit cost reports are being developed.

E. Criteria for Inclusion of Business Areas in the Fund

The criteria established for a business area to be considered for inclusion are:

- Identification of outputs (the products or services provided).
- A cost accounting system to collect costs of producing outputs.
- Identification of customers to pay for outputs so resources can be aligned in the account of the requirement.

The DoD Comptroller has initiated task groups for each business area in the Fund and a number of additional functional areas throughout the Department. The task groups for existing business areas will validate outputs of the business area, ensure that unit cost resourcing principles are being followed to determine the cost of producing the outputs, and develop and implement additional financial management tools as necessary to improve the business operations. The task groups focusing on new functional areas will review candidate functions based on the criteria described above. Task group membership includes representatives from DoD Comptroller, other OSD organizations such as Production and Logistics and Force, Manpower and Personnel, the Service Assistant Secretaries (Financial Management), the Comptrollers of Defense Agencies, as well as functional and financial personnel from Service major commands.

The identification of costs to the organization's outputs establishes the organization as a unit cost activity. The resultant unit cost, or cost per output, is used as a management, productivity, and budgetary tool at all levels of the Department. Two types of unit cost allocation methodologies, process costing and job costing, are used to generate the cost per output.

1. Process Costing. This type of methodology assumes a continuous, homogeneous output stream. This assumption is

important since the objective is to calculate the average cost per output. In order to calculate an average cost which closely approximates the actual, outputs have to take place continuously and require essentially the same method and level of effort to produce. Second, the outputs chosen to measure each business area must be non-controllable on the part of the producers. This puts producers in the position of having to minimize costs because this is the only variable at their control, not the requirement to produce the output itself. The method to calculate unit cost is to identify the direct costs and add appropriate prorated shares of indirect costs and general and administrative overhead costs, and divide the total by workload for a specified time period. The budget for such activities lists unit cost, or average cost per output, goals which, when multiplied by the number of work units produced, provides earned cost authority. Earned authority is then assessed against actual costs incurred to measure performance. Process costing cannot be applied to functions where broadly defined average cost targets cannot be successfully established, and even if they were, the results would not be meaningful.

2. Job Costing. This type of costing methodology applies to outputs which are dissimilar in nature, and require different methods and levels of effort to produce. Such systems, referred to as job costing, are common in DoD and have been successfully used in a wide range of support activities, primarily those previously managed under industrial fund financial management. The budget for DoD business areas measured based on job costing specifies the average change in costs (plus or minus) that can be incurred across the whole range of outputs compared to the previous year. The budget also lists the expected yearend net operating result (NOR). Specifying a net operating result and measuring actual results against that NOR goal ensures that the activity operates within the approved profit/loss margins for the year.

III. POLICY AND REGULATORY DEVELOPMENT RESPONSIBILITIES

A. DoD Comptroller

Financial policies for the Fund are established by the DoD Comptroller. The Fund operates under the same policies and procedures previously used for other revolving funds with the incorporation of additional guidance (described in Section IV) to accommodate implementation of the Fund. Policy and procedural changes are coordinated through the Directorate for Business Management, which reports to the DoD Deputy Comptroller for Management Systems. Input comes from the Military Services, Defense Agencies, and all Office of Secretary of Defense (OSD) functional directorates, as well as DoD Comptroller staff offices. All policy initiatives that affect management, budgeting, and accounting within the Fund are filtered through this Directorate for development, review, and/or coordination.

B. **Defense Business Operations Fund Financial Policies Board**

To ensure Military Department and Defense Agency involvement in the management of the Fund, a Defense Business Operations Fund Financial Policies Board was established concurrent with implementation of the Fund. The Board is chaired by the Principal Deputy Comptroller of DoD, and includes Service and Agency financial and functional representatives as well as representatives from other OSD offices. The Board is used as a forum in which the representatives can exchange information on their problems and experiences. The Board also provides a vehicle for reviewing policy and procedure proposals, and making recommendations prior to final policy decisions. The Defense Business Operations Fund Financial Policies Board ensures wide corporate participation as Department vision and philosophy is integrated with policy.

C. **Component Heads**

Implementation of the Fund's policies and procedures is the responsibility of the Military Department Secretaries and the heads of the other DoD Components. While broad policies for the Fund are developed and issued by DoD Comptroller, Component heads are expected to drive these policy decisions down through their organizations to ensure local level managers are properly informed and operating under the concepts of the Fund. The Components recognize this responsibility, and have established, to varying degrees, internal organizations which specifically oversee the implementation of the Fund within their respective Component.

The Army has established their own Defense Business Operations Fund Board of Directors, or the Army Board, whose mission is to promote implementation, coordination, standardization, and understanding of all matters relating to the Fund within the Army. The Army Board forwards recommendations to their representative on the DoD Defense Business Operations Fund Financial Policies Board. These recommendations are based on a review of potential alternative strategies and improvements to the concepts, planning, regulations and operations of the Fund. The Army Board is chaired by the Comptroller of the Army, and includes representatives from the major commands and other senior staff management officials.

While the Navy, Air Force and Defense Agencies have not established formal boards of their own, each has identified a group within their respective budget offices charged with dealing specifically with Fund issues and overseeing implementation. Similar to the Army, these organizations work directly with either the major commands or field level activities to facilitate lower level participation and operation.

Implementation of procedures by the Components also includes responsibility for issuing lower level budgetary authority in

consonance with the resourcing provided by the DoD Comptroller. Components provide the financial goals to each level of activity managed in the Fund. Allocation to the major command level has already been accomplished by each Component. We are continuing to work in conjunction with the Services and Agencies in allocating the goals to lower level field activities. As outlined in Section IV, the process of formulating budgets is undergoing revision to institutionalize unit cost. The schedules published in the Budget Guidance Manual will be changed for preparation of the FY 1994/1995 President's budget.

IV. POLICY AND PROCEDURES

A. Policy and Regulatory Guidance

The Fund operates under existing financial policies in place for industrial funds and stock funds, as well as additional interim policy guidance contained in August 19 and September 27, 1991, DoD Comptroller memoranda. Additional guidance or clarification of existing guidance, as applicable, is issued to disseminate standard policies that address requirements for all business areas included in the Fund and to ensure consistent and successful implementation of policies. The DFAS issued implementing procedures for these policies. DoD plans to incorporate applicable financial management policy into a single DoD publication.

B. Policy and Procedure Improvements Implemented

As indicated above, operations of the Fund are based on policies and procedures that have been in effect for stock and industrial funds. However, a number of management, accounting, policy, and procedural changes have already been implemented. The following paragraphs describe the intent of the changes, as well as actions underway to fully implement the procedures.

1. Execution Budgets for Activities Previously Industrially Funded. In keeping with the Department's desire to decentralize management and empower the decision makers at every level, the Components are encouraged to issue unit cost goals at the lowest level where costs are incurred. Prior to FY 1992, industrial fund activities were not issued funding documents. They received their obligational authority from customer orders. Now, while costs incurred must still be based on the receipt of customer orders, "operating budgets" provide official management cost goals and have been issued to the Services and Agencies. As with the private sector, the type of goal depends on the nature of the business. Some unit cost goals are established at the Component business area level; some activities have so many outputs that the goals are expressed in terms of the change in cost from the prior year; other activities have goals expressed in terms of cost per billable hour. At this time, the Components are still in the process of issuing the goals to the individual

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activities. When this process is completed, many managers in the field will know, for the first time, what higher level management expects of them from a cost management and financial performance standpoint.

2. Unit Cost Budgets for New Revolving Fund Activities. For FY 1992, Congress approved the inclusion of the Defense Finance and Accounting Service, Defense Technical Information Center, Defense Reutilization and Marketing Service, Defense Industrial Plant Equipment Center, and the Defense Commissary Agency in the Fund. These business areas, which were previously funded with annual fixed amounts based on estimates of work load, are now funded principally on the basis of the actual work load that is performed. While this is a new process for most business areas, there is no doubt that this resource methodology will improve cost consciousness.

3. Minor Construction Funding Procedures. Minor construction projects costing $15,000 or more will be funded through the capital budget. These minor construction projects will then be depreciated by the business area in accordance with the capital asset accounting guidance. Reflecting minor construction projects in the capital budget conforms to GAO principles and guidelines. This approach is reflected in the FY 1993 budget submission.

4. Funding of Central Design Activities and Other Software Acquisitions. Previously these efforts, when accomplished by in-house activities, were treated as operating costs. However, the development of new software should be subject to economic analysis, and treated as an investment, regardless of where software development is accomplished. During review of the Amended FY 1992/1993 President's budget, the decision was made to move these costs to the capital budget. This requires depreciation of software releases in accordance with capital asset accounting procedures. This change was put into effect in FY 1992, and is reflected in the FY 1993 budget submission.

5. Air Mobility Command (AMC) Funding Procedures and Budget Presentation. Although AMC was included in the industrial fund for over 20 years, the nature of its operations did not lend itself to total recovery of costs through rate structure revenue. AMC's costs are primarily driven by the requirement to keep its crews ready for contingencies, as with any other aviation warfighting organization. The opportunity exists for the Department to take advantage of the capability and capacity that are generated as a byproduct of AMC's mission training. Because the primary mission of the C-5 and C-141 is not to carry packages in peacetime, the actual cost per ton mile is more expensive than on commercial carriers. However, with the aircraft flying anyway, there is in reality no, or minimal, additional cost to DoD for most of the cargo carried by AMC.

The Department uses the AMC rate structure to optimize utilization of the cargo capac:· In general, rates are

established to match those on commercial carriers. By charging for this "no cost" service, the higher air (as compared to surface) transportation costs prevent all cargo from suddenly becoming air eligible. The difference between the revenue AMC generates and costs AMC incurs is covered by direct appropriations to Operation and Maintenance (O&M) account for Air Force.

Although the circumstance described above is not new, the previous budget presentation and budget execution procedure did not provide visibility to managers and review levels, including the Congress, of the total costs of AMC in a single location in the budget. To protect the financial condition of the industrial fund, some categories of costs were financed in that account via rates, and others were financed by direct appropriation. Industrial fund costs were presented in terms of cost per ton mile, although that is not what drives the costs, and nowhere in the budget presentation could one see the total cost of AMC.

Now, all of the costs of AMC will be financed through the Fund. Costs of the primary output will be expressed, justified, and managed in terms of the cost to train and maintain the capability of a crew, rather than in terms of the cost of a ton mile. Rates will continue to be based on those of the commercial carriers, and the difference between revenue and cost will be financed as a direct appropriation in O&M, Air Force. This improvement was implemented in FY 1992, and is reflected in the FY 1993 budget submission.

6. Capital Budgeting. Probably the most significant initiative reflected in the Fund is the inclusion of capital budgeting. Under this policy, business budgets are segregated into operating and capital budgets. Any investment in equipment, software, minor construction, and other management improvements costing $15,000 or more is funded through the capital budget and its costs amortized or depreciated over a predetermined period. The $15,000 criteria is based on congressional actions on expense/investment criteria. Approval by the Congress of a capital surcharge in FY 1992 has provided the mechanism for a gradual increase in the level of investment in these businesses. Previous levels have approximated less than two percent of sales.

Each business area will have a separate capital budget, which, as a minimum, will be separated into the following categories:

A. Minor Construction Projects under $300,000

B. ADP Equipment Purchases

C. Other Equipment Purchases

D. Software Development

E. Other Capital Investments

Each capital investment will be capitalized and depreciated in accordance with the capital asset accounting policies discussed elsewhere in this paper. Consistent with congressional direction, separate cash general ledger accounts have been established to segregate those transactions related to capital revenues (collected from surcharges and depreciation) and capital disbursements. Also, as directed by the Congress, sufficient cash will be maintained at all times in separate capital general ledger accounts to cover the unliquidated obligations.

The Congress rejected the Department's proposal to fund military construction projects through the Defense Business Operations Fund Capital Budget. However, the Department will continue to make decisions on military construction projects as if they were included in the Fund. During the internal DoD budget formulation process, construction projects will be included in the Fund submission. The Revolving Fund Directorate in the Program Budget office will have responsibility for review of those projects. Current plans are to include the construction projects in the capital budgets of the Fund, in future submissions to Congress. This will provide additional information and insight to the Fund reviewers on the congressional staff without affecting the appropriation process. The appropriation and authorization process will continue to be included in the military construction request in accordance with the congressional action on the FY 1992 request.

Regardless of where the construction projects are funded, depreciation on those projects will be fully reflected in the operating costs and rates of the Fund businesses. This policy is reflected in the FY 1993 budget submission, and will be put into effect in FY 1993 for all businesses in the Fund. Inclusion of all depreciation in the rates will improve the consistency of cost proposals in competitive situations. Because of the competition policy now in effect in Depot Maintenance, activities engaged in that business were directed to include depreciation of facilities in their costs in FY 1992. A standard depreciation period of 20 years has been prescribed for depreciation of construction projects. Although a shorter period than the useful life of most projects, the 20 years was considered to be as far beyond the DoD planning window as it is prudent to go. In addition, the use of a uniform period at the outset of this change in policy will improve the chances of successful implementation.

7. Mobilization/Surge Costs. A change in pricing policy reflected in the FY 1993 budget changes the way costs related to mobilization and excess surge capacity for wartime requirements will be funded, as they are identified. This policy applies to those costs incurred at an activity that will insure that the activity will meet the mobilization/surge requirements that it

has been given; costs which would not be incurred to satisfy customer peacetime requirements. Examples of costs included in this category are: maintenance of facilities, when those facilities are in excess of peacetime requirements; purchase of war reserve materiel; and purchase of materiel in excess of peacetime requirements to maintain an industrial base.

These mobilization costs will be funded through direct appropriations to the Operations and Maintenance account of the parent Service or Agency. The prices of outputs of these activities are to reflect peacetime operating costs only. Customers of the Fund will pay the cost of the items being procured (including overhead), and thus should be faced with more consistent pricing between competing activities. Similarly, there will be better visibility, to decision makers at every level, of those costs included in the DoD budget for surge or readiness requirements.

8. Ownership and Accountability of Assets. The assets of the former industrial and stock funds have been capitalized to the Component business areas of the Fund. Accountability of these assets is in accordance with current DoD regulations that govern the stock and industrial funds. All capital assets used by Fund activities are depreciated or amortized in accordance with capital asset accounting guidance and generally accepted accounting standards.

DoD has established a Capital Asset Accounting working group which is responsible for reviewing policies and procedures and making recommendations to enhance management and control of capital assets in the Fund.

9. Depreciation. All capital assets owned by activities in the Fund will be depreciated or amortized by the individual Component business area. Procedures will be in accordance with schedules, specified time frames, and criteria to be provided in capital assets accounting guidance. All assets will be inventoried and capitalized to the appropriate business area, depreciation/amortization schedules will be developed or continued, and depreciation expenses will be recorded in the financial records. These procedures will be followed regardless of the source of acquisition funding for the asset.

In FY 1992, cost of operations for activities that were previously industrially funded included funded depreciation on all assets, including those that had previously been acquired through the Asset Capitalization Program. Cost of operations in FY 1992, for business areas that were previously unit costed and had capital budgets, included funded depreciation on assets installed as of October 1, 1990. Additionally, business areas new to the revolving fund in FY 1992 included in their cost of operations funded depreciation on all assets installed after October 1, 1991. Additionally business areas that were previously unit costed, or are new to the Fund, recorded in the

financial records unfunded depreciation on all other assets identified and capitalized in FY 1992.

In FY 1993, cost of operations for all Fund activities will include funded depreciation on all capital assets regardless of funding source, year of installation, or year of capitalization.

10. Full recovery of costs. Pricing guidance is consistent with long standing DoD policy calling for break-even operation of certain business functions within the Department. Previous stock and industrial fund operations were expected to break even over the long term. In actuality, prior year operations have at times resulted in substantial losses remaining on the financial records over a number of years. Management philosophy and focus under the Fund has reaffirmed the Department's policy for budgeting on a breakeven basis. As a result, prices in future budget submissions will be uniformly established to recover the full cost of operations, including recovery of prior year losses or return of prior year gains, by the end of the budget year.

All businesses in the Fund are required to set their prices based upon full cost recovery. Prices or rates, as appropriate, remain fixed during the year; actual costs are evaluated against established prices; and the financial condition assessed accordingly. Profits or losses will be determined at the end of the year and reflected in price adjustments to the customers in a subsequent year. Establishing rates based on costs assists individual program managers (customers) in making cost effective program decisions. Such decisions may involve selecting among alternative goods or services, choosing from competitive sources providing similar goods or services, or determining whether to replace or to repair an item. Assessing the financial health of the Fund through the evaluation of financial results will improve the emphasis on the cost of doing business and ultimately reduce the prices charged to the operating forces, and thus the cost of those forces.

Prices for all business areas in the Fund are set to produce an accumulated operating result (AOR) of zero in FY 1993. This should eliminate the need for passthroughs, which have previously been used to recover losses. Also, by setting prices to recover losses or refund gains, visibility over the effect that each business area has on the performance of the Fund will be maintained. Alternatively, using a passthrough to recover a loss would be undesirable since it would be made to the Fund, and the performance of individual business areas would be obscured.

V. EDUCATION AND TRAINING

A. Overview

Since the initiation of the Fund, significant actions have been taken to provide the Military Services and Defense Agencies

information on developmental issues as well as specific policies and procedures. In part, this information is made available in the form of DoD Comptroller memoranda and changes to DoD regulations and procedures discussed elsewhere in this plan. Other actions, such as briefings, workshops and training classes, have become a routine and essential part of the information flow.

B. Briefings and Other Informational Forums

The DoD Comptroller staff has developed much information on the implementation and operation of the Fund and unit cost resourcing. One way that has been used extensively to communicate this information is the presentation of briefings by the DoD Comptroller staff. Such briefings were delivered in a number of forums and have reached thousands of DoD managers and employees over the past year. Another major method used is the Unit Cost Resourcing Task Groups. These groups include Service Secretary and major command level personnel who are responsible for implementing the Fund as well as unit cost resourcing within their own Component. Other forums have also been used to present information about the Fund including American Society of Military Comptrollers conferences and Professional Development Institute workshops, and briefings and lectures held at Services' schools, e.g., Professional Military Comptroller's School, Naval Postgraduate School, Defense Systems Management College, and the Army Management Engineering College.

The DoD Comptroller staff will continue to brief interested groups, but alternative media are required to reach a wider audience and are being pursued. A video briefing is planned for development to explain the Fund's goals, policies and implementation processes. Also planned for publication and distribution are other forms of easily exportable information such as pamphlets and educational aids for delivery via diskette.

C. Training and Education

In December 1990 DoD Comptroller launched the financial management education and training initiative. The objective of this initiative is to revitalize and define the universe of financial management education and training. This education and training is critical to the successful implementation of DoD-wide systems and core principles common to financial management across all Components. A catalog of education and training offerings was developed, the financial management work force was surveyed and an advisory board structure was developed to analyze current and future training needs in the financial management community. Through this process, training needs will be reviewed, new materiels as required will be added, and duplicative course work eliminated.

The DoD Comptroller staff has undertaken an initiative specifically focused on developing new methods needed to support implementation of the Fund and unit cost resourcing. This effort is led by DoD Comptroller staff and involves the spectrum of DoD

training and educational institutions. The formal process ommenced at an April 1992 meeting of representatives of the DoD financial management educational community. The purpose of this meeting was to identify current curricula, review the curricula quality control process, define specific training requirements, and develop resources and strategies to address those training needs.

VI. SUMMARY OF BENEFITS

The expanded use of businesslike financial practices and the establishment of a management structure designed to encourage the reduction of production cost will benefit the mission customer foremost. At the same time, the DoD's ability to better manage its resources will be improved. The specific benefits of the Fund are summarized below:

- A customer-provider relationship is developed between the customer (normally the operating forces) and the provider (the support activity). This relationship allows customers to determine the level/quantity of support they need to perform their mission. Support activities will produce goods or provide services to meet customer demand.

- The Fund provides the customers a true picture of their support costs, thereby allowing them to make more informed decisions. The more functions that are included in the Fund, the closer DoD moves to mission budgeting.

- DoD managers are encouraged to focus on performance and cost management by increasing emphasis on business operations and deemphasizing cash management.

- The Fund will be instrumental in providing DoD managers at all levels a supportive financial system that produces useful and timely financial management information.

- The customer, the most appropriate organization to determine requirements, justifies support funding.

- Stabilizing prices to customers through the Fund helps ensure that approved programs are executed as planned.

- Overall accounting work load is lessened, without reducing visibility of costs, due to lessening of fiscal (cash) transfers internal to the Fund. Procedures are being developed to allow the recognition and recording of revenue and expenses by each business area in the Fund for certain types of reciprocal interchanges, without the exchange of cash or recording of obligations. Intrafund transactions will be utilized instead of the more expensive and time consuming expenditure transactions reconciliation processes used today.

- Capital budgeting provides visibility of the true total cost of an operation and allows both the customer and review organizations (i.e., the Services, OSD and Congress) to make more informed decisions. It also provides a mechanism to determine whether the expected benefits of the decision are realized. Total cost management helps production managers weigh investment needs to achieve optimum results for the resources expended. The manager can determine whether investment will help achieve long-term lower costs and provide more incentive to make that investment.

- Minimal new procedures were required to implement the newly established Defense Business Operations Fund because DoD has been in the revolving fund business since 1951. There are existing cost accounting systems, which when modified to accept the new requirements and controls, will continue to serve local managers in a more efficient and expanded capacity.

- By linking support activity funding to customer requirements, rather than prior year expenditures, we will change many managers' previous mind-set of spending every dollar available to them this year for fear that they may not get as much next year.

- The expanded cost visibility increases all managers' accountability for their decisions. Customers will provide justification as to why programs are required; the Fund activities will provide information on their efficiency and effectiveness.

- The ability of Congress to influence or exercise oversight will be improved through the separation of the customers and the suppliers. Congress will receive better information about the nature and the cost of DoD activities under review. Financial statements will provide operations and investment cost information that will not only show how much is being spent to perform support missions, but also how efficiently the missions are being performed.

- Savings resulting from better business practices that are encouraged by the Fund will reduce expenditures, maintain levels of readiness and service, and absorb staff reductions driven by increasingly constrained budgets. Every dollar saved in the support establishment, while still providing the same quality level of support, means another dollar overall available to meet national security requirements within the reduced funding levels of DoD.

VII. CONCLUSION

The Fund provides the Department with the resource management structure required by support organizations to ensure that mission customers are provided the best possible product or

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service at the lowest cost. The Department is aggressively pursuing all actions required to ensure prudent and rational implementation of the Fund. Successful implementation of the Fund will yield improved capabilities to the Department. The existing financial structure, with necessary interim policies and procedures, provides a solid framework for establishing sound business management practices.

Improvement requires constant attention and promotes change to the established way of doing business. We must continue to search for alternative ways to meet the Department's performance and quality goals at minimum cost.

DEFENSE BUSINESS OPERATIONS FUND

PRINCIPAL STATEMENTS

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Principal Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

ASSETS	1992
1. **Financial Resources:**	
a Fund Balances with Treasury	$4,134,600,298
b. Cash	27,506
c. Foreign Currency	
d. Other Monetary Assets	
e. Investments, Non-Federal	
f. Accounts Receivable, Net - Non-Federal	469,277,332
g. Inventories Held for Sale, Net	79,318,762,158
h. Loans Receivable, Net - Non-Federal	1,576,155,313
i. Advances and Prepayments, Non-Federal	1,164,405,031
j Property Held for Sale	
k. Other, Non-Federal	1,425,370,512
l. *Intragovernmental Items:*	
(1) Accounts Receivable, Federal	6,106,265,974
(2) Loans Receivable, Federal	
(3) Investments, Federal	
(4) Other, Federal	225,191,610
m. **Total Financial Resources**	$94,420,005,734
2. **Non-Financial Resources:**	
a. Resources Transferable to Treasury	
b. Inventories Not Held for Sale	9,261,339,298
c. Property, Plant and Equipment, Net	11,352,346,969
d. Other	3,097,835,973
e. **Total Non-Financial Resources**	$23,711,522,240
3. **Total Assets**	$118,131,527,974
LIABILITIES	
4. **Funded Liabilities**	
a. Accounts Payable, Non-Federal	6,813,942,805
b. Accrued Interest Payable	
c. Accrued Payroll and Benefits	1,016,372,689
d. Accrued Entilement Benefits	3,958,807
e. Lease Liabilities	673,593
f. Debt	
g. Guarantees Payable	
h. Other Funded Liabilities, Non-Federal	111,608,290

The accompanying notes are an integral part of these statements.

II-4 Principal Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Principal Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

LIABILITIES Continued	1992
i. Intragovernmental Liabilities	
(1) Accounts Payable, Federal	$3,742,675,818
(2) Debt	1,576,155,313
(3) Deferred Revenue	334,635,605
(4) Other Funded Liabilities, Federal	1,314,302,255
j Total Funded Liabilities	$14,914,325,175
5 Unfunded Liabilities:	
a. Accrued Leave	215,028,796
b. Lease Liabilities	
c. Pensions and Other Actuarial Liabilities	
d. Other Unfunded Liabilities	929,327,498
e. Total Unfunded Liabilities	$1,144,356,294
6. TOTAL LIABILITIES	$16,058,681,469
NET POSITION	
7. Fund Balances:	
a. Revolving Fund Balances	103,213,401,594
b. Trust Fund Balances	
c. Appropriated Fund Balances	
d. Total Fund Balances	$103,213,401,594
8. Less Future Funding Requirements	1,140,554,733
9. Net Position	$102,072,846,861
10. Total Liabilities and Net Position	$118,131,528,330

The accompanying notes are an integral part of these statements.

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Principal Statements
Statement of Operations (and Changes in Net Position)
for Period Ended September 30, 1992
(Dollars)

REVENUES AND FINANCING SOURCES	1992
1. Appropriations Expensed	$3,424,200,000
2. Revenues from Sales of Goods	
a. To the Public	6,496,906,936
b. Intragovernmental	63,727,671,408
3. Interest and Penalties, Non-Federal	
4 Interest, Federal	
5. Taxes	
6. Other Revenues and Financing Sources	45,199,697,088
7. Less: Taxes and Receipts Returned to the Treasury	
8. *Total Revenues and Financing Sources*	$118,848,475,432
EXPENSES	
9. Cost of Goods or Services Sold	
a. To the Public	5,197,338,177
b. Intragovernmental	54,247,148,475
10. Program or Operation Expenses	18,150,504,617
11. Depreciation	789,707,784
12. Bad Debts and Write-offs	26,603,083
13. Interest	
a. Federal Financing Bank/Treasury Borrowing	
b. Federal Securities	
c. Other	16,527,148
14. Other Expenses	40,274,762,222
15. Total Expenses	$118,702,591,506
16. Excess (Shortage) of revenues and Financing Sources Over Total Expenses Before Adjustments	145,883,926
17. Plus (Minus) Adjustments:	
a. Extraordinary Items	(848,316,409)
b. Prior Period Adjustments	2,148,268,018
18. Excess (Shortage) of Revenues and Financing Sources over Total Expenses	$1,445,835,535
19. Plus: Unfunded Expenses	122,088,036
20. Excess (Shortage) of Revenues and Financing Sources Over Funded Expenses	$1,567,923,571

The accompanying notes are an integral part of these statements.

II-6 Principal Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Principal Statements
Statement of Operations (and Changes in Net Position)
for Period Ended September 30, 1992
(Dollars)

EXPENSES Continued	1992
21. Net Position, Beginning Balance	
22. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	$1,417,936,423
23. Plus (Minus) Equity Transfers	100,667,603,274
24. Net Position, Ending Balance	$102,085,539,697

The accompanying notes are an integral part of these statements.

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Principal Statements
Statement of Cash Flows (Indirect)
for the Period Ended September 30, 1992
(Dollars)

Cash Flows from Operating Activities:	1992
1. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	$1,445,835,535
Adjustments affecting Cash Flow:	
2. Appropriations Expensed	(10,509,137,247)
3. Decrease (Increase) in Accounts Receivable	(1,532,094,846)
4. Decrease (Increase) in Loans Receivable	
5. Decrease (Increase) in Other Assets	(1,907,181,593)
6. Increase (Decrease) in Accounts Payable	793,973,847
7. Increase (Decrease) in Debt	
8. Increase (Decrease) in Other Liabilities	409,736,644
9 Depreciation and Amortization	789,707,784
10. Other Unfunded Expenses	1,911,400,136
11. Other Adjustments	499,430,884
12. Total Adjustments	($9,544,164,391)
13. Net Cash Provided (Used) by Operating Activities	($8,098,328,856)
Cash Flows from Non-Operating Activities:	
14. Proceeds from Sales of Investments	
15. Proceeds from Sales of Property, Plant and Equipment	
16. Purchases of Investments	
17. Purchases of Property, Plant and Equipment	695,091,650
18. Net Cash Provided (Used) by Non-Operating Activities	($695,091,650)
CASH PROVIDED (USED) BY FINANCIAL ACTIVITIES	
19. Appropriations (Current Warrants)	3,424,200,000
20. Add:	
a. Restorations	
b. Transfers of Cash from Others	6,493,606,441
21. Deduct:	
a. Withdrawals	
b. Transfers of Cash to Others	2,623,296,344
22. Net Appropriations	$7,294,510,097

The accompanying notes are an integral part of these statements.

II-8 Principal Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Principal Statements
Statement of Cash Flows (Indirect)
for the Period Ended September 30, 1992
(Dollars)

CASH PROVIDED (USED) BY FINANCIAL ACTIVITIES Continued	1992
23. Borrowing from the Public	
24. Repayments on Loans	
25. Borrowing from the Treasury and the Federal Financing Bank	
26. Repayments on Loans from the Treasury and the Federal Financing Bank	$1,527,883,970
27. Other Borrowings and Repayments	
28. Net Cash Provided (Used) by Financing Activities	5,766,626,127
29. Net Cash Provided (Used) by Operating, Non-Operating and Financing Activities	(3,026,794,379)
30. Fund Balance with Treasury, Cash, and Foreign Currency, Beginning	
31. Fund Balance with Treasury, Cash, and Foreign Currency, Ending	($3,026,794,379)

The accompanying notes are an integral part of these statements.

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Principal Statements
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Dollars)

Program Name (s)	BUDGET Resources	Obligations Direct	Obligations Reimbursed	ACTUAL Expenses
Army	$11,784,546,103		$11,337,771,707	$29,481,879,940
Navy	27,568,008,715		25,116,754,791	41,843,021,248
Air Force	15,747,935,684	$205,956,938	16,741,174,661	26,144,267,610
Defense Agencies	13,164,116,709		11,743,228,559	13,849,759,698
CISA & DITSO	1,487,140,799		1,335,576,302	1,422,941,350
DFAS Financial OPS	651,299,753		688,860,168	536,738,562
DECA	7,128,119,802		7,348,306,173	7,084,937,247
Joint Log Corp Acct	294,942,337		320,256,635	7,295,628
Totals	$68,264,607,211	$205,956,938	$64,938,929,718	$111,318,928,496

Budget Reconciliation

A. Total Expenses	$111,318,928,496
B. Add:	
(1) Capital Acquisitions	696,366,132
(2) Loans Disbursed	
(3) Other Expended Budget Authority	(16,458,279,906)
C. Less:	
(1) Depreciation and Amortization	784,340,933
(2) Unfunded Annual Leave Expense	109,291,706
(3) Other Unfunded Expenses	21,730,267,743
D. Expended Appropriations	$94,772,673,789
E. Less Reimbursements	74,762,609,218
F. Expended Appropriations, Direct	$20,010,064,571

The accompanying notes are an integral part of these statements.

DEFENSE BUSINESS OPERATIONS FUND

COMBINING STATEMENTS

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

ASSETS	Departmental	Army	Navy	Air Force	Defense Agencies
1. Financial Resources:					
a. Fund Balances with Treasury	$6,645,976,731	($1,070,325,311)	$272,162,281	($1,172,439,574)	($399,018,180)
b. Cash				27,506	
c. Foreign Currency					
d. Other Monetary Assets					
e. Investments, Non-Federal					
f. Accounts Receivable, Net - Non-Federal		7,594,417	117,659,189	92,970,394	125,616,437
g. Inventories Held for Sale, Net		13,169,229,981	18,104,627,123	36,236,964,453	11,004,418,684
h. Loans Receivable, Net - Non-Federal			1,576,155,313		
i. Advances and Prepayments, Non-Federal		53,593,113	599,942,120	162,156,553	347,936,856
j. Property Held for Sale					
k. Other, Non-Federal		438,543	1,421,091,365	3,840,604	
l. Intragovernmental Items:					
(1) Accounts Receivable, Federal		483,728,642	1,592,405,185	1,090,059,390	2,248,584,771
(2) Loans Receivable, Federal					
(3) Investments, Federal					
(4) Other, Federal		571,578	195,901,345	9,810,338	
m. Total Financial Resources	$6,645,976,731	$12,644,830,963	$23,879,943,921	$36,423,389,664	$13,327,538,568
2. Non-Financial Resources:					
a. Resources Transferable to Treasury					
b. Inventories Not Held for Sale		1,756,844,685	842,877,896	6,660,147,769	1,468,948
c. Property, Plant and Equipment, Net		2,839,866,234	6,220,044,514	1,900,499,827	111,660,092
d. Other		2,797,105,210	278,383,689		7,543,646
e. Total Non-Financial Resources		$7,393,816,129	$7,341,306,099	$8,560,647,596	$120,672,686
3. Total Assets	$6,645,976,731	$20,038,647,092	$31,221,250,020	$44,984,037,260	$13,448,211,254

IV-4 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

ASSETS	DISA	DFAS Fin Ops	DECA	Joint Logistics	Total
1. Financial Resources:					
a. Fund Balances with Treasury	$50,413,178	$120,954,990	($298,836,530)	($14,287,287)	$4,134,600,298
b. Cash					27,506
c. Foreign Currency					
d. Other Monetary Assets					
e. Investments, Non-Federal					
f. Accounts Receivable, Net - Non-Federal	559,227	170,000	124,657,668		469,227,332
g. Inventories Held for Sale, Net			803,521,917		79,318,762,158
h. Loans Receivable, Net - Non-Federal					1,576,155,313
i. Advances and Prepayments, Non-Federal	31,383	533,062	211,944		1,164,405,031
j. Property Held for Sale					
k. Other, Non-Federal					1,425,370,512
l. Intragovernmental Items:					
(1) Accounts Receivable, Federal	349,749,908	46,800,200	287,270,722	7,667,156	6,106,265,974
(2) Loans Receivable, Federal					
(3) Investments, Federal					
(4) Other, Federal	2,543,801			16,364,548	225,191,610
m. Total Financial Resources	$403,297,497	$168,458,252	$916,825,721	$9,744,417	$94,420,005,734
2. Non-Financial Resources:					
a. Resources Transferable to Treasury					
b. Inventories Not Held for Sale					9,261,339,298
c. Property, Plant and Equipment, Net	167,382,108	111,729,351	1,164,843		11,352,346,969
d. Other	14,803,428				3,097,835,973
e. Total Non-Financial Resources	$182,185,536	$111,729,351	$1,164,843		$23,711,522,240
3. Total Assets	$585,483,033	$280,187,603	$917,990,564	$9,744,417	$118,131,527,974

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

LIABILITIES	Departmental	Army	Navy	Air Force	Defense Agencies
4. Funded Liabilities					
a. Accounts Payable, Non-Federal		$731,659,729	$3,543,404,853	$906,719,394	$393,342,213
b. Accrued Interest Payable					
c. Accrued Payroll and Benefits		79,226,860	802,407,307	91,079,425	18,121,485
d. Accrued Entitlement Benefits			906,010	3,052,797	
e. Lease Liabilities					
f. Debt					
g. Guarantees Payable					
h. Other Funded Liabilities, Non-Federal		12,556	90,875,331	6,920,403	
i. Intragovernmental Liabilities					
(1) Accounts Payable, Federal		819,005,654	1,120,646,537	369,202,598	1,054,263,970
(2) Debt			1,576,155,313		
(3) Deferred Revenue		66,336,888	29,803,741	55	238,494,921
(4) Other Funded Liabilities, Federal			680,171,450	631,041,880	3,088,925
j. Total Funded Liabilities		$1,696,241,687	$7,844,370,542	$2,008,016,552	$1,707,311,514
5. Unfunded Liabilities:					
a. Accrued Leave		72,012,781		33,724,309	61,397,832
b. Lease Liabilities					
c. Pensions and Other Actuarial Liabilities					
d. Other Unfunded Liabilities		929,327,498			
e. Total Unfunded Liabilities		$1,001,340,279		$33,724,309	$61,397,832
6. TOTAL LIABILITIES		$2,697,581,966	$7,844,370,542	$2,041,740,861	$1,768,709,346

IV-6 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

LIABILITIES	DISA	DFAS Fin Ops	DECA	Joint Logistics	Total
4. Funded Liabilities					
a. Accounts Payable, Non-Federal	$312,542,840	$26,420,033	$899,853,743		$6,813,942,805
b. Accrued Interest Payable					
c. Accrued Payroll and Benefits	8,890,394	3,907,184	12,740,034		1,016,372,689
d. Accrued Entitlement Benefits					3,958,807
e. Lease Liabilities	673,593				673,593
f. Debt					
g. Guarantees Payable					
h. Other Funded Liabilities, Non-Federal	13,800,000				111,608,290
i. Intragovernmental Liabilities					
(1) Accounts Payable, Federal	13,457,926	67,004,671	292,154,416	6,940,046	3,742,675,818
(2) Debt					1,576,155,313
(3) Deferred Revenue					334,635,605
(4) Other Funded Liabilities, Federal					1,314,302,255
j. Total Funded Liabilities	$349,364,753	$97,331,888	$1,204,748,193	$6,940,046	$14,914,325,175
5. Unfunded Liabilities:					
a. Accrued Leave		20,104,399	27,789,475		215,028,796
b. Lease Liabilities					
c. Pensions and Other Actuarial Liabilities					
d. Other Unfunded Liabilities					929,327,498
e. Total Unfunded Liabilities		$20,104,399	$27,789,475		$1,144,356,294
6. TOTAL LIABILITIES	$349,364,753	$117,436,287	$1,232,537,668	$6,940,046	$16,058,681,469

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

NET POSITION	Departmental	Army	Navy	Air Force	Defense Agencies
7. Fund Balances:					
a. Revolving Fund Balances	$6,645,976,731	$18,338,603,844	$23,376,879,475	$42,976,021,066	$11,740,899,740
b. Trust Fund Balances					
c. Appropriated Fund Balances					
d. Total Fund Balances	$6,645,976,731	$18,338,603,844	$23,376,879,475	$42,976,021,066	$11,740,899,740
8. Less Future Funding Requirements		997,538,718		33,724,309	61,397,832
9. Net Position	$6,645,976,731	$17,341,065,126	$23,376,879,475	$42,942,296,757	$11,679,501,908
10. Total Liabilities and Net Position	$6,645,976,731	$20,038,647,092	$31,221,250,017	$44,984,037,618	$13,448,211,254

IV-8 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Financial Position
as of September 30, 1992
(Dollars)

NET POSITION	DISA	DFAS Fin Ops	DECA	Joint Logistics	Total
7. Fund Balances:					
a. Revolving Fund Balances	$236,18,280	$182,855,715	($286,757,629)	$2,804,372	$103,213,401,594
b. Trust Fund Balances					
c. Appropriated Fund Balances					
d. Total Fund Balances	$236,18,280	$182,855,715	($286,757,629)	$2,804,372	$103,213,401,594
8. Less Future Funding Requirements		20,104,399	27,789,475		1,140,554,733
9. Net Position	$236,118,280	$162,751,316	($314,547,104)	$2,804,372	$102,072,846,861
10. Total Liabilities and Net Position	$585,483,033	$280,187,033	$917,990,584	$9,744,418	$118,131,528,330

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Operations (and Changes in Net Position)
for Period Ended September 30, 1992
(Dollars)

REVENUES AND FINANCING SOURCES	Departmental	Army	Navy	Air Force	Defense Agencies
1. Appropriations Expensed	$3,424,200,000				
2. Revenues from Sales of Goods					
a. To the Public		$40,048,141	$270,559,019	$170,057,750	$10,302,717
b. Intragovernmental		9,664,519,991	27,445,186,260	11,368,785,472	13,100,064,716
3. Interest and Penalties, Non-Federal					
4. Interest, Federal					
5. Taxes					
6. Other Revenues and Financing Sources		19,800,894,956	12,140,414,673	13,210,296,705	28,018,476
7. Less: Taxes and Receipts Returned to the Treasury					
8. Total Revenues and Financing Sources	$3,424,200,000	$29,505,463,088	$39,856,159,952	$24,749,139,927	$13,138,405,909
EXPENSES					
9. Cost of Goods or Services Sold					
a. To the Public		39,317,830	94,599,983		10,302,717
b. Intragovernmental		8,841,489,294	27,136,296,095	5,929,981,159	10,113,723,864
10. Program or Operation Expenses	648,533,367	3,757,998,265	2,094,912,550	6,933,036,558	3,178,076,473
11. Depreciation		125,985,201	497,246,399	133,315,167	924,669
12. Bad Debts and Write-offs		9,195,551		17,407,410	31
13. Interest					
a. Federal Financing Bank/Treasury Borrowing					
b. Federal Securities					
c. Other					
14. Other Expenses		16,707,893,799	12,347,641,081	10,644,628,930	547,394,013
15. Total Expenses	$648,533,367	$29,481,879,940	$42,170,696,108	$23,658,369,843	$13,850,421,767

IV-10 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Operations (and Changes in Net Position)
for Period Ended September 30, 1992
(Dollars)

REVENUES AND FINANCING SOURCES	DISA	DFAS Fin Ops	DECA	Joint Logistics	Total
1. Appropriations Expensed					$3,424,200,000
2. Revenues from Sales of Goods					
a. To the Public	$917,655		$6,085,021,654		6,496,906,936
b. Intragovernmental	1,335,690,288	$651,299,753	152,004,928	$10,100,000	63,727,671,408
3. Interest and Penalties, Non-Federal					
4. Interest, Federal					
5. Taxes					
6. Other Revenues and Financing Sources			20,072,278		45,199,697,088
7. Less: Taxes and Receipts Returned to the Treasury					
8. Total Revenues and Financing Sources	$1,336,607,943	$651,299,753	$6,177,098,860	$10,100,000	$118,848,475,432
EXPENSES					
9. Cost of Goods or Services Sold					
a. To the Public			5,053,117,647		5,197,338,177
b. Intragovernmental	1,249,019,394		976,638,669		54,247,148,475
10. Program or Operation Expenses	24,244,482	493,171,135	1,013,236,159	7,295,628	18,150,504,617
11. Depreciation	18,289,632	13,837,078	109,638		789,707,784
12. Bad Debts and Write-offs			91		26,603,083
13. Interest					
a. Federal Financing Bank/Treasury Borrowing					
b. Federal Securities					
c. Other	64,649	9,625,950	6,835,930		16,527,148
14. Other Expenses		20,104,399	7,100,000		40,274,762,222
15. Total Expenses	$1,291,618,157	$536,738,562	$7,057,038,134	$7,295,628	$118,702,591,506

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Operations (and Changes in Net Position)
for Period Ended September 30, 1992
(Dollars)

	Departmental	Army	Navy	Air Force	Defense Agencies
16. Excess (Shortage) of revenues and Financing Sources Over Total Expenses Before Adjustments	$2,775,666,633	$23,583,148	($2,314,536,156)	$1,090,770,084	($712,015,858)
17. Plus (Minus) Adjustments:					
a. Extraordinary Items			(341,425,055)	46,687,291	(553,578,645)
b. Prior Period Adjustments		24,989,352	(8,689,784)	2,264,726,434	(1,434,791)
18. Excess (Shortage) of Revenues and Financing Sources over Total Expenses	$2,775,666,633	$48,572,500	($2,664,650,995)	$3,402,183,809	($1,267,029,294)
19. Plus: Unfunded Expenses		9,195,551		27,426,538	61,397,832
20. Excess (Shortage) of Revenues and Financing Sources Over Funded Expenses	$2,775,666,633	$57,768,051	($2,664,650,995)	$3,429,610,347	($1,205,631,462)
21. Net Position, Beginning Balance					
22. Excess (Shortage) of Revenues and Financing Sources Sources Over Total Expenses	2,775,666,633	48,572,500	(2,664,650,995)	3,402,183,810	(1,267,029,294)
23. Plus (Minus) Equity Transfers	3,870,310,097	17,292,492,626	26,054,223,308	39,540,112,947	12,946,531,202
24. Net Position, Ending Balance	$6,645,976,730	$17,341,065,126	$23,389,572,313	$42,942,296,757	$11,679,501,908

IV-12 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Operations (and Changes in Net Position)
for Period Ended September 30, 1992
(Dollars)

	DISA	DFAS Fin Ops	DECA	Joint Logistics	Total
16. Excess (Shortage) of revenues and Financing Sources Over Total Expenses *Before Adjustments*	$44,989,786	$114,561,191	($879,939,274)	$2,804,372	$145,883,926
17. Plus (Minus) Adjustments:					
a. Extraordinary Items					(848,316,409)
b. Prior Period Adjustments	(131,323,193)				2,148,268,018
18. Excess (Shortage) of Revenues and Financing Sources over Total Expenses	($86,333,407)	$114,561,191	($879,939,274)	$2,804,372	$1,445,835,535
19. Plus: Unfunded Expenses	18,289,632	33,677,596	(27,899,113)		122,088,036
20. Excess (Shortage) of Revenues and Financing Sources Over Funded Expenses	($68,043,775)	$148,238,787	($907,838,387)	$2,804,372	$1,567,923,571
21. Net Position, Beginning Balance					
22. Excess (Shortage) of Revenues and Financing Sources Sources Over Total Expenses	(86,333,407)	114,561,191	(907,838,387)	2,804,372	1,417,936,423
23. Plus (Minus) Equity Transfers	322,451,687	48,190,124	593,291,283		100,667,603,274
24. Net Position, Ending Balance	$236,118,280	$162,751,315	($314,547,104)	$2,804,372	$102,085,539,697

Department/Agency: Department of Defense
Reporting Entity: *Defense Business Operations* Fund *Combining Statements*
Statement of Cash Flows (Indirect)
for the Period Ended September 30, 1992
(Dollars)

Cash Flows from Operating Activities:	Departmental	Army	Navy	Air Force	Defense Agencies
1. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	$2,775,666,633	$48,572,500	($2,664,650,997)	$3,402,183,810	($1,267,029,294)
Adjustments affecting Cash Flow:					
2. Appropriations Expensed	(3,424,200,000)				
3. Decrease (Increase) in Accounts Receivable		(107,638,550)	(482,058,275)	411,045,709	(834,068,469)
4. Decrease (Increase) in Loans Receivable					
5. Decrease (Increase) in Other Assets		(1,817,507,019)	2,014,417,434	(627,136,805)	(663,119,235)
6. Increase (Decrease) in Accounts Payable		29,777,615	(372,934,313)	23,834,775	(371,531,438)
7. Increase (Decrease) in Debt					
8. Increase (Decrease) in Other Liabilities		(17,728,242)	826,117,095	(336,410,949)	(77,767,607)
9. Depreciation and Amortization		125,985,204	497,246,399	133,315,167	924,669
10. Other Unfunded Expenses		9,195,551	1,744,888,864	27,426,538	81,884,671
11. Other Adjustments		1,178,132,325	262,457,771	(4,203,424,238)	2,740,055,411
12. Total Adjustments	($3,424,200,000)	($599,783,119)	$4,490,125,972	($4,571,349,803)	$876,377,952
13. Net Cash Provided (Used) by Operating Activities	($648,533,367)	($551,210,619)	$1,825,474,975	($1,169,165,993)	($390,651,342)
Cash Flows from Non-Operating Activities:					
14. Proceeds from Sales of Investments					
15. Proceeds from Sales of Property, Plant and Equipment					
16. Purchases of Investments					
17. Purchases of Property, Plant and Equipment		519,114,693	86,630,574	3,245,718	8,366,838
18. Net Cash Provided (Used) by Non-Operating Activities		($519,114,693)	($86,630,574)	($3,245,718)	($8,366,838)

IV-14 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Cash Flows (Indirect)
for the Period Ended September 30, 1992
(Dollars)

Cash Flows from Operating Activities:	DISA	DFAS Fin Ops	DECA	Joint Logistics	Total
1. Excess (Shortage) of Revenues and Financing Sources Over Total Expenses	($86,333,407)	$114,561,192	($879,939,274)	$2,804,372	$1,445,835,535
Adjustments affecting Cash Flow:					
2. Appropriations Expensed			(7,084,937,247)		(10,509,137,247)
3. Decrease (Increase) in Accounts Receivable	(52,587,569)	(46,970,200)	(412,140,333)	(7,667,156)	(1,532,094,846)
4. Decrease (Increase) in Loans Receivable					
5. Decrease (Increase) in Other Assets	7,858,041	(533,062)	(804,796,399)	(16,364,548)	(1,907,181,593)
6. Increase (Decrease) in Accounts Payable	192,454,350	93,424,703	1,192,008,159	6,940,046	793,973,847
7. Increase (Decrease) in Debt					
8. Increase (Decrease) in Other Liabilities	(28,910,346)	3,907,184	40,529,509		409,736,644
9. Depreciation and Amortization	18,289,632	13,837,078	109,638		789,707,784
10. Other Unfunded Expenses		20,104,399	27,899,113		1,911,400,136
11. Other Adjustments			522,209,615		499,430,884
12. Total Adjustments	$137,104,108	$83,770,102	($6,519,117,945)	($17,091,658)	($9,544,164,391)
13. Net Cash Provided (Used) by Operating Activities	$50,770,701	$198,331,294	($7,399,057,219)	($14,287,286)	($8,098,328,856)
Cash Flows from Non-Operating Activities:					
14. Proceeds from Sales of Investments					
15. Proceeds from Sales of Property, Plant and Equipment					
16. Purchases of Investments					
17. Purchases of Property, Plant and Equipment	357,523	77,376,304			695,091,650
18. Net Cash Provided (Used) by Non-Operating Activities	($357,523)	($77,376,304)			($695,091,650)

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Cash Flows (Indirect)
for the Period Ended September 30, 1992
(Dollars)

	Departmental	Army	Navy	Air Force	Defense Agencies
CASH PROVIDED (USED) BY FINANCIAL ACTIVITIES					
19. Appropriations (Current Warrants)	$3,424,200,000				
20. Add:					
a. Restorations					
b. Transfers of Cash from Others	6,493,606,441				
21. Deduct:					
a. Withdrawals					
b. Transfers of Cash to Others	2,623,296,344				
22. Net Appropriations	$7,294,510,097				
23. Borrowing from the Public					
24. Repayments on Loans					
25. Borrowing from the Treasury and the Federal Financing Bank					
26. Repayments on Loans from the Treasury and the Federal Financing Bank			$1,527,883,970		
27. Other Borrowings and Repayments					
28. Net Cash Provided (Used) by Financing Activities	7,294,510,097		(1,527,883,970)		
29. Net Cash Provided (Used) by Operating, Non-Operating and Financing Activities	6,645,976,730	(1,070,325,312)	210,960,431	(1,172,411,711)	(399,018,180)
30. Fund Balance with Treasury, Cash, and Foreign Currency, Beginning					
31. Fund Balance with Treasury, Cash, and Foreign Currency, Ending	$6,645,976,730	($1,070,325,312)	$210,960,431	($1,172,411,711)	($399,018,180)

IV-16 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Cash Flows (Indirect)
for the Period Ended September 30, 1992
(Dollars)

	DISA	DFAS Fin Ops	DECA	Joint Logistics	Total
CASH PROVIDED (USED) BY FINANCIAL ACTIVITIES					
19. Appropriations (Current Warrants)					$3,424,200,000
20. Add:					
a. Restorations					
b. Transfers of Cash from Others					6,493,606,441
21. Deduct:					
a. Withdrawals					
b. Transfers of Cash to Others					2,623,296,344
22. Net Appropriations					$7,294,510,097
23. Borrowing from the Public					
24. Repayments on Loans					
25. Borrowing from the Treasury and the Federal Financing Bank					
26. Repayments on Loans from the Treasury and the Federal Financing Bank					
27. Other Borrowings and Repayments					1,527,883,970
28. Net Cash Provided (Used) by Financing Activities					5,766,626,127
29. Net Cash Provided (Used) by Operating, *Non-Operating and Financing Activities*	50,413,178	120,954,990	(7,399,057,219)	(14,287,286)	(3,026,794,379)
30. Fund Balance with Treasury, Cash, and Foreign Currency, Beginning					
31. Fund Balance with Treasury, Cash, and Foreign Currency, Ending	$50,413,178	$120,954,990	($7,399,057,219)	($14,287,286)	($3,026,794,379)

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Dollars)

	BUDGET			ACTUAL
		Obligations		
Program Name (s)	Resources	Direct	Reimbursed	Expenses
Army	$11,784,546,103		$11,337,771,707	$29,481,879,940
Navy	27,568,008,715		25,116,754,791	41,843,021,248
Air Force	15,747,935,684	$205,956,938	16,741,174,661	26,144,267,610
Defense Agencies	13,164,116,709		11,743,228,559	13,849,759,698
CISA & DITSO	1,487,140,799		1,335,576,302	1,422,941,350
DFAS Financial OPS	651,299,753		688,860,168	536,738,562
DECA	7,128,119,802		7,348,306,173	7,084,937,247
Joint Log Corp Acct	294,942,337		320,256,635	7,295,628
Totals	$68,264,607,211	$205,956,938	$64,938,929,718	$111,318,928,496

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Budget Reconciliation

A. Total Expenses	$111,318,928,496
B. Add:	
(1) Capital Acquisitions	696,366,132
(2) Loans Disbursed	
(3) Other Expended Budget Authority	(16,458,279,906)
C. Less:	
(1) Depreciation and Amortization	784,340,933
(2) Unfunded Annual Leave Expense	109,291,706
(3) Other Unfunded Expenses	21,730,267,743
D. Expended Appropriations	$94,772,673,789
E. Less Reimbursements	74,762,609,218
F. Expended Appropriations, Direct	$20,010,064,571

IV-18 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements (Army)
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992

Program	BUDGET			ACTUAL
		Obligations		
Name (s)	Resources	Direct	Reimbursed	Expenses
Depot Maint/Other	$3,024,168,789.32	$0.00	$1,848,773,708.29	$2,004,236,013.26
Depot Maint/Ordnance	1,141,927,505.60	0.00	623,570,262.38	689,348,467.21
Depot Dist.	3,539,698.40	0.00	197,393,523.32	182,998,397.86
Supply Mgmt.	7,167,599,189.95	0.00	8,187,044,224.82	26,127,306,744.23
Transportation	447,310,919.74	0.00	480,989,988.07	477,990,317.74
Totals	$11,784,546,103.01	$0.00	$11,337,771,706.88	$29,481,879,940.30

Budget Reconciliation

A. Total Expenses	$29,481,879,940.30
B. Add:	
(1) Capital Acquisitions	519,114,692.52
(2) Loans Disbursed	
(3) Other Expended Budget Authority	(19,119,940,854.99)
C. Less:	
(1) Depreciation and Amortization	125,985,201.00
(2) Unfunded Annual Leave Expense	
(3) Other Unfunded Expenses	9,195,551.44
D. Expended Appropriations	$10,745,873,025.39
E. Less Reimbursements	9,568,169,238.26
F. Expended Appropriations, Direct	$1,177,703,787.13

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements (Navy)
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Dollars)

Program Name (s)	BUDGET			ACTUAL
		Obligations		
	Resources	Direct	Reimbursed	Expenses
AVIATION	2,472,209,266		2,022,167,235	3,097,477,056
ORDNANCE	651,826,176		699,582,097	877,458,677
SHIPYARD	4,406,417,202		4,118,702,659	5,428,536,303
MARINE CORPS	355,868,779		195,941,506	181,167,810
DIST DEPOT	531,115,892		531,115,892	401,037,304
SUPPLY MGMT	6,481,488,527		6,481,488,527	20,654,672,765
TRANSPORTATION	3,150,582,954		2,817,660,469	2,920,960,716
BASE SUPPORT	1,390,259,464		1,476,930,889	1,492,753,255
INFO SERVICES	310,231,478		286,617,752	287,226,196
PRINTING	185,814,317		292,323,681	284,972,013
R&D	7,632,194,660		6,219,609,747	6,216,759,153
Totals	$27,568,008,715		$25,142,140,454	$41,843,021,248

Budget Reconciliation

A. Total Expenses	$41,843,021,248
(1) Capital Acquisitions	86,630,574
(2) Loans Disbursed	
(3) Other Expended Budget Authority	6,842,062
C. Less:	
(1) Depreciation and Amortization	491,989,186
(2) Unfunded Annual Leave Expense	
(3) Other Unfunded Expenses	13,831,195,145
D. Expended Appropriations	$27,613,309,553
E. Less Reimbursements	27,587,321,441
F Expended Appropriations, Direct	$25,988,112

IV-20 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements (Air Force)
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Dollars)

	BUDGET			ACTUAL
		Obligations		
Program Name (s)	Resources	Direct	Reimbursed	Expenses
Depot Maint	$4,731,698,833		$3,766,694,154	$3,571,476,177
Dist Depot			4,628,899	64,550,568
Supply Mgmt	7,832,684,713	$205,956,938	9,870,798,985	19,361,780,017
Transportation	3,181,547,148		3,094,366,436	3,139,421,437
Base Support	2,004,990		4,686,187	7,039,411
Totals	$15,747,935,684	$205,956,938	$16,741,174,661	$26,144,267,610

Budget Reconciliation

A. Total Expenses	$26,144,267,610
B. Add:	
(1) Capital Acquisitions	3,245,718
(2) Loans Disbursed	
(3) Other Expended Budget Authority	2,392,843,912
C. Less:	
(1) Depreciation and Amortization	133,315,167
(2) Unfunded Annual Leave Expense	
(3) Other Unfunded Expenses	7,699,819,099
D. Expended Appropriations	$20,707,222,974
E. Less Reimbursements	16,268,176,920
F. Expended Appropriations, Direct	$4,439,046,054

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements (Defense Logistics Agency)
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Dollars)

Program Name (s)	BUDGET Resources	Obligations Direct	Obligations Reimbursed	ACTUAL Expenses
Distribution Depots	$724,294,932		$1,241,211,744	$1,159,287,555
Supply Management	11,989,577,061		10,008,649,328	12,325,462,870
Industrial Plant Equip	25,403,222		39,627,462	39,060,392
Reutiliztion & Marketing	320,960,033		375,000,286	280,171,628
Technical Information	44,673,015		44,673,015	11,923,551
Clothing Factory	59,208,446		34,066,724	33,853,702
Totals	$13,164,116,709		$11,743,228,559	$13,849,759,698

Budget Reconciliation

A. Total Expenses	$13,849,759,698
B. Add:	
(1) Capital Acquisitions	8,366,838
(2) Loans Disbursed	
(3) Other Expended Budget Authority	
C. Less:	
(1) Depreciation and Amortization	924,669
(2) Unfunded Annual Leave Expense	61,397,832
(3) Other Unfunded Expenses	1,141,097,625
D. Expended Appropriations	$12,654,706,410
E. Less Reimbursements	13,164,116,709
F. Expended Appropriations, Direct	($509,410,299)

IV-22 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements (DISA)
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Dollars)

	BUDGET			ACTUAL
		Obligations		
Program Name (s)	Resources	Direct	Reimbursed	Expenses
DISA-DITSO	$66,503,509		$66,503,509	$60,786,187
DISA-CISA	1,420,637,290		1,269,072,793	1,362,155,163
Totals	$1,487,140.799		$1,335,576,302	$1,422,941,350

Budget Reconciliation

A. Total Expenses	$1,422,941,350
B. Add:	
(1) Capital Acquisitions	357,523
(2) Loans Disbursed	
(3) Other Expended Budget Authority	
C. Less:	
(1) Depreciation and Amortization	18,289,632
(2) Unfunded Annual Leave Expense	
(3) Other Unfunded Expenses	130,696,819
D. Expended Appropriations	$1,274,312,422
E. Less Reimbursements	1,335,576,302
F. Expended Appropriations, Direct	($61,263,880)

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements (DFAS)
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Dollars)

	BUDGET			ACTUAL
		Obligations		
Program Name (s)	Resources	Direct	Reimbursed	Expenses
DFAS	$651,299,753		$698,860,169	$536,738,562
Totals	$651,299,753		$698,860,169	$536,738,562

Budget Reconciliation

A. Total Expenses	$536,738,562
B. Add:	
(1) Capital Acquisitions	
(2) Loans Disbursed	77,376,304
(3) Other Expended Budget Authority	
C. Less:	
(1) Depreciation and Amortization	13,837,078
(2) Unfunded Annual Leave Expense	20,104,399
(3) Other Unfunded Expenses	
D. Expended Appropriations	$580,173,389
E. Less Reimbursements	651,299,753
F. Expended Appropriations, Direct	($71,126,364)

IV-24 Combining Statements

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements (Defense Commissary Agency)
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Nearest Dollar)

	BUDGET			ACTUAL
		Obligations		
Program Name (s)	Resources	Direct	Reimbursed	Expenses
Commissary Operations	$995,819,802	$1,098,860,991	$15,719,802	$1,055,180,931
Commissary Resale Stocks	6,132,300,000	6,233,725,380		6,029,756,316
Totals	$7,128,119,802	$7,332,586,371	$15,719,802	$7,084,937,247

Budget Reconciliation:

A. Total Expenses	$7,084,937,247
B. Add:	
(1) Capital Acquisitions	1,274,482
(2) Loans Disbursed	
(3) Other Expended Budget Authority	261,974,975
C. Less:	
(1) Depreciation and Amortization	109,638
(2) Unfunded Annual Leave Expenses	27,789,475
(3) Other Unfunded Expenses	59,361,129
D. Expended Appropriations	$7,260,926,462
E. Less Reimbursements	6,194,213,403
F Expended Appropriations, Direct	$1,066,713,059

Department/Agency: Department of Defense
Reporting Entity: Defense Business Operations Fund Combining Statements (Joint Logistics Systems Center)
Statement of Budget and Actual Expenses
for the Period Ended September 30, 1992
(Dollars)

Program Name (s)	BUDGET Resources	BUDGET Obligations Direct	BUDGET Obligations Reimbursed	ACTUAL Expenses
Joint Logistics Systems Center	$306,696,459		$294,942,337	$7,295,628
Totals	$306,696,459		$294,942,337	$7,295,628

Budget Reconciliation

A. Total Expenses	$7,295,628
B. Add:	
(1) Capital Acquisitions	
(2) Loans Disbursed	
(3) Other Expended Budget Authority	
C. Less:	
(1) Depreciation and Amortization	
(2) Unfunded Annual Leave Expense	
(3) Other Unfunded Expenses	
D. Expended Appropriations	$7,295,628
* E. Less Reimbursements	(6,264,548)
F. Expended Appropriations, Direct	$13,560,176

*Includes $16,364,548 in Progress Payments for work to be billed at a later date.

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Part VI - Management Comments

OFFICE OF THE COMPTROLLER OF THE DEPARTMENT OF DEFENSE

WASHINGTON DC 20301-1100

JUN 16 1993

MEMORANDUM FOR INSPECTOR GENERAL, DEPARTMENT OF DEFENSE

SUBJECT: Draft Reports on Internal Controls and Compliance with Laws and Regulations for the Defense Business Operations Fund (DBOF) Financial Statements for FY 1992 (Project No. 2FG-2008)

This is in reply to your memorandum of May 27, 1993, requesting comments concerning draft audit reports on the Defense Business Operations Fund (DBOF) financial statements for FY 1992.

Comments to the subject draft report are attached. Due to the extensiveness of the draft report and the limited period of time provided to review the extensive findings, it was not feasible to provide detailed responses to each finding in the draft report. In some cases, additional information from various other audits referenced in the draft report, as well as a review of such other referenced audits, is required in order to permit this office to provide a more detailed response to specific findings.

This office is concerned that the DoDIG's findings on "Inadequate Audit Trails" imply that the DoDIG considers anything less than the transmission, or availability, of the entire DBOF transaction data base to, or at, respectively, Departmental levels is unacceptable from an internal controls and audit trail perspective. This office strongly objects to such an implication. The more traditional practice of transmitting summary financial reporting information to Departmental level activities, while retaining the more detailed supporting data at local installations, is a longstanding practice that has been widely acceptable not only within the Department of Defense, but throughout the Federal Government and the private sector as well. In addition, the Compliance findings on "Monthly Report of Operations" and "OMB Bulletin 93-02" reference outdated, and therefore, misleading information to arrive at incorrect conclusions.

My point of contact on these draft audit reports is Mr. Oscar Covell. He may be reached at (703) 697-6149.

Alvin Tucker
Acting Chief Financial Officer

Attachment

INSPECTOR GENERAL, DEPARTMENT OF DEFENSE,
"DRAFT REPORT ON INTERNAL CONTROLS AND COMPLIANCE WITH LAWS AND REGULATIONS FOR THE DEFENSE BUSINESS OPERATIONS FUND (DBOF) FINANCIAL STATEMENTS FOR FY 1992"
(PROJECT NO. 2FG-0028)

DEPARTMENT OF DEFENSE COMMENTS

* * * * *

FINDINGS

PART II INTERNAL CONTROLS

TRANSACTIONS NOT PROPERLY RECORDED AND ACCOUNTED FOR

- DODIG Finding: Inadequate Controls Over Cash. The DODIG could not verify cash balances on the Consolidating, Combining, and Business Area Financial Statements for the DBOF FY 1992 financial statements because three of the five Defense Finance and Accounting Service (DFAS) Centers were using improper accounting procedures. Additionally, they identified a material discrepancy between cash balances reported by the DBOF and Department of the Treasury (Treasury) records.

  The DoDIG could not confirm the DBOF cash transactions reported by the DFAS-Denver Center because accounting procedures used did not provide adequate separation of suspense account transactions made for the DBOF from transactions made for the Air Force General Fund (appropriation account no. 57X6875). These procedures resulted in commingling of the DBOF transactions with Air Force transactions. The reported balance in the overall Air Force suspense account for FY 1992 was $614.0 million in collections and $633.0 million in disbursements; however the DBOF portion of these transactions could not be determined. In addition, the DoDIG found that the DFAS-Denver Center, on occasion, improperly reported estimates of its transactions rather than actual totals on its Statements of Transactions (DD Form 1329) and its Statements of Accountability (SF 1219) forwarded to the Treasury. Responsible managers at the DFAS-Denver Center stated that they used an estimate of cash transactions whenever they had not received the required transaction information from its disbursing offices in time to prepare their report to the Treasury. The use of estimates for these reports is not authorized by DoD or Treasury guidance, and does not provide an accurate assessment of cash transactions.

  Accounting procedures used by the DFAS-Indianapolis Center and the DFAS-Cleveland Center precluded net disbursements,

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totaling $2.7 million and $26.0 million, respectively, from being identified to the proper DBOF business area.

The DoDIG also found a material discrepancy in the year-end cash balances between DBOF financial statements and Treasury records. According to the DoD's Form and Content guidance, which was issued on December 30, 1992, the cash balances at the consolidating and business area level should equal the difference between cash disbursements and cash collections during the fiscal year. The DoDIG identified a variance of approximately $649.0 million between what Treasury reported as a reduction to the DBOF appropriation ($3.160 billion) and what the business area financial statements reported on the Fund Balance with Treasury account ($2.511 billion). Likewise, there was a $649.0 million variance in what Treasury reported as Current Year Appropriations at the end of FY 1992 ($7.295 billion) and what the DBOF Combining Statements presented as Fund Balance with Treasury, Departmental ($6.646 billion). The DoDIG was able to trace the $649.0 million discrepancy to four business areas:

- Army Force Supply Management
- Air Force Supply Management
- Defense Supply Management
- Navy Distribution Depot

At the conclusion of the audit field work, the auditors still had not determined the cause of the discrepancy.

<u>DoD RESPONSE</u>: Partially concur. Concur that the practice of commingling Defense Business Operations Fund (97X4930) and other DoD funds representing undistributed disbursement and collection transactions is improper and that it is also improper to report estimated cash transactions on the Statement of Transactions (DD Form 1329) and the Statement of Accountability (SF 1219). It is noted that the reporting of estimated cash transactions to the Treasury is not a function of the Business Operations Fund even though the practice does affect the matching of DBOF unliquidated obligations with expenditures.

The lack of information in the finding precludes this office from commenting on the accounting procedures at either the DFAS-Indianapolis or Cleveland Centers.

Nonconcur with the reported variance of $649.0 million. The variance of $649M is derived by subtracting the reported Final Balance with Treasury ($2.511B) reported on financial statements from the reduction to the DBOF appropriation ($3.160B) is a misstatement of fact. First, the Fund Balance with Treasury as supported by the Financial

Statements is not $2.522 billion, but $4.1 billion. Second, the "reduction" to the DBOF appropriation is actually the Net Outlays from the appropriation and will almost never result in the Fund Balance with Treasury since this calculation does not consider, Beginning Balance, Transfers-In, or Transfers Out. While the DBOF had no Beginning Balance, there were Transfers-In and Transfers-Out that should have been considered in computing the Fund Balance with Treasury. The amount that the auditors claim Treasury reported as Current Year Appropriations (7.295 billion) is neither Current Year Appropriations nor Fund Balance with Treasury.

DoD guidance on form and content of October 27, 1992, advised that the Treasury balance was held at the DoD Comptroller level and that a combining statement would be prepared showing DoD Component balances, the Departmental (DoD Comptroller) Fund Balances with Treasury, and that the sum of those would equal the Fund Balance With Treasury reported by the Treasury Department. The DBOF Fund Balance With Treasury shown on the Combining Statement, and the Principal Statements, as of September 30, 1992, was $4,134,600,298.

- DODIG Finding: **Transactions For and By Others Not Recorded in a Timely Manner.** Timing differences in recording transactions resulted in variances between the DFAS Centers and the business areas. The financial statements for each business area must exclude Transactions For Others and include Transactions By Others. The transactions for and by others are not recorded at the business area level until the transactions have been reviewed and accepted. This lag in reporting causes discrepancies between financial data at the DFAS Centers and operating data at the business areas and results in "unmatched" buyer and seller transactions, unliquidated obligations, and undistributed balances. The variances overstate accounts receivable and understate accounts payable at the business areas. The DoDIG found subsidiary records did not support $2.95 billion of unliquidated obligations recorded in the Defense Fuel Supply Center (DFSC) trial balance portion of the Defense Logistics Agency Supply Management business area. The DFAS and the DFSC did not ensure the accuracy and completeness of the recorded obligations. Also, the subsidiary records were not available in sufficient detail to support $492.7 million of undistributed disbursements and $356.1 million of undistributed collections.

  DoD RESPONSE: Partially Concur. Undistributed disbursements and collections at the DoD Component departmental level are applied against accounts payable and accounts receivable at the departmental level. However, disbursements and collections that have been identified and

distributed by the departmental level, but are not recorded in the same reporting period at the DBOF activity level, will result in an under/overstatement of accounts payable and receivable at the DoD Component DBOF activity level. The reference in the finding to unsupported unliquidated obligations, and that DFAS and DFSC did not ensure the accuracy of recorded transactions, is not supported by the facts in the finding.

- DODIG Finding: Improper Elimination or Reporting of Intrafund Transactions. Approximately $17.7 billion of intrafund transactions among business areas of the DBOF are not properly identified or eliminated from the FY 1992 DBOF Combining or Consolidated financial statements. This is a result of the lack of specific DBOF controls and policies regarding the treatment of these transactions. In addition, the present accounting systems used to record disbursements and collections are not designed to identify and retain the intrafund data when both the buyer and seller are DBOF activities. Due to the lack of guidance and inadequate accounting systems, The DoDIG was unable to determine what amount of intrafund transactions should have been eliminated or disclosed in the DBOF financial statements. The DoD Comptroller estimated $17.7 billion in intrafund transactions for the DBOF during FY 1992.

  DoD RESPONSE: Concur. DBOF Intrafund Policy has not been published. Until such policy is issued, changes to DoD's accounting systems to identify and record intrafund transactions should not be made.

- DODIG Finding: Depreciation Computations Incorrect. Depreciation schedules had not been developed for capital assets throughout the reporting entities. This caused many of the entities to incorrectly report depreciation. The DoD 7220.9-M, DoD Accounting Manual, prescribes depreciation guidance and subsequent policies and procedures included in the DoD Comptroller's memorandum on "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992, require that depreciation be computed using the straight-line method. The straight-line method is based on the original acquisition cost or reasonable estimate divided equally among accounting periods during the asset's useful life. For example, Army Depot Maintenance personnel did not accurately compute depreciation of fixed assets, both because personnel recorded incorrect information and because personnel did not have an accounting system that allowed them to compute depreciation. The Air Force Depot Maintenance did not depreciate capital assets at their useful lives because Air Force depreciation policy did not agree with the guidance memorandum issued by the DoD

Comptroller. As a result, depreciation was understated by $9.7 million.

DoD RESPONSE: Concur in principle. The Department agrees that some of the Defense Agencies do not have an adequate property system to compute depreciation accurately and in a mechanized mode. The Department is in the process of integrating the Installation Equipment Management System (IEMS) with the Defense Business Management System to achieve a capability to process property transactions, including depreciation, on a transaction basis. However, it should be noted that the Business Operations Fund reported depreciation expense in FY 1992 of $789.7 million of which the reported understatement of $9.7 million is approximately 1.2 percent.

- DODIG Finding: Accounts Receivable Not Confirmed and Revenue Not Recognized. Accounts receivable and revenue balances were misstated due to inaccurate accounting entries and lack of controls in place to properly record these entries. Specifically, the Air Force Depot Maintenance did not recognize at least $274.0 million in revenue associated with work completed as of September 30, 1992. It also had inaccurate journal voucher entries of $221.0 million to the accounts receivable and the progress billings account. Also, the Air Force Transportation revenue was not always processed for billing. The Air Force Audit Agency found about $9.6 million of revenue earned for the movement of passengers, cargo and mail on established routes, was not billed. Finally, the Air Force Base Support accounting controls were not in place to record revenue and receivable transactions in the correct accounting period. As a result, revenue of $7.2 million and accounts receivable of $1.2 million may be materially misstated.

  DoD RESPONSE: Concur. Revenue should be recognized and reported in accordance with current guidance; and accounts receivable should be accurately recorded and collected. It is noted that the revenue of $7.2, and $1.2 of accounts receivable, applies to the Air Force Base Support business area, not DBOF as a whole.

- DODIG Finding: Liabilities Not Properly Accounted For. Liabilities of the DBOF were misstated due to the lack of accounting controls and the failure of accounting personnel to follow the DoD 7220.9-M, "DoD Accounting Manual." The Navy's Military Sealift Command business area had estimated invalid accruals of $38.1 million for Charter Hire, $145.2 million for Cargo, and $38.1 million for supplies and services. The invalid accrual amounts were accrued in the wrong year, not adequately liquidated, and improperly written off. Additionally, the Air Force Audit Agency found

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that Air Force Supply Management, Fuel Division purchases, and disbursements to foreign governments were not properly accounted for. The Air Force Fuel Division did not record or pay for fuel purchases away from home and did not report $3.8 million of off-station fuel purchases in the period when the transaction occurred. Also, the Air Force Base Support did not reconcile accounts payable balances to unpaid bills. The payroll accrual procedures did not ensure accurate recording of payroll transactions or correct adjusting entries for payroll expenses to actual amounts. Also, accounting controls were not in place for recording all valid payroll transactions in plant financial records and reporting payroll transactions in the correct accounting period. As a result, $2.6 million of payables could not be substantiated.

DoD RESPONSE: Concur. Liabilities for accounts payable should be accrued in the period incurred and reconciled to subsidiary accounts.

ASSETS NOT SAFEGUARDED AGAINST LOSS FROM UNAUTHORIZED USE

- DODIG Finding: Lack of Supporting Documentation. Our substantive testing on the Fund Balance with Treasury account identified a lack of supporting documentation. The DoD Directive, 5015.2, Records Management Program, March 22, 1991, requires the DoD Components to establish and maintain a central Records Management Program to ensure that DoD records are maintained and managed from creation through disposal. The DoDIG determined subsidiary records were not available to support adjustments of $2.74 billion in the DFSC Statement of Cash Flows and $1.14 billion of other unfunded expenses in the Division's Statement of Budget and Actual Expenses. Army Transportation accounts receivable balances of about $23.7 million did not have supporting documentation, and the accounts payable subsidiary ledger incorrectly contained debit balances of about $112.0 million with no documentation to support the recorded entries. Furthermore, the Army Transportation financial statement contained $28.0 million of unsupported adjustments. The Navy's Military Sealift Command could not adequately support transactions of $29.2 million for maintenance and repair and other per diem items, $74.0 million for cargo, and $191.7 million for supplies and services. The Air Force Supply Management made adjusting entries totaling $75.0 million and the Fuel Division of Supply Management paid fuel vouchers totaling $6.8 million without required supporting documents. As a result, $167.0 million in accounting adjustments or related account balances reported in the Air Force financial statements were not substantiated. The Air Force Audit Agency also found that the Air Force Depot Maintenance business area made incorrect or unsupported entries totaling

$112.2 million to year-end contract inventory accounts on the financial statements because Depot Maintenance had not established effective procedures for making adjusting entries. As a result, the $843.3 million of Inventory Not Held For Sale could not be substantiated on the Air Force Depot Maintenance Statement of Financial Position.

DoD RESPONSE: Concur in principle. Based on the information presented, it is clear that there is a substantial lack of supporting documentation. A more in-depth assessment of the impact of this deficiency is required before the Department can take a final position on the causes of the discrepancy and effect corrective actions.

- DODIG Finding: Capital Assets and Inventory Not Valued Correctly and Existence Is Uncertain. The valuation methods of reporting assets and inventory on the DBOF financial statements were not consistently applied throughout the business areas. Also, physical inventories were not performed or reconciled to the financial records. The DoD Accounting Manual, DoD 7220.9-M, requires physical inventories of personal property to verify the existence of property recorded in general ledger accounts and provides detailed guidance on reconciling general ledger inventory accounts to subsidiary property records. The DoD 7220.9-M also provides criteria for capitalizing assets; however, the threshold for asset capitalization has been increased to $15,000 by the "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992. The DoD 7200.14-M, "Department of Defense Accounting and Reporting of Government Property Lost, Damaged, or Destroyed," May 16, 1977, also provides procedures for reconciling differences as a result of physical counts. The DoDIG found that the DFAS Centers did not reconcile and match the physical inventory to the financial records for capital assets. Also, The DoDIG found the property, plant and equipment account classification presented on the DFAS business area financial statements was understated by $13.3 million. In addition, the Defense Commissary Agency (DeCA), Resale Stocks business area did not ensure that approximately $800.0 million of inventory recorded on the general ledger agreed with the subsidiary ledgers.

  The Army Depot Maintenance business area did not properly capitalize $87.2 million of fixed assets. Assets and liabilities were overstated by $70.0 million and $4.0 million, respectively, because two depot activities were included in the FY 1992 statements although they are no longer Army Depot Maintenance activities. The Navy's DBOF fixed assets recorded in the financial statements could not be located. The DBOF inventory records Were inaccurate, and some fixed assets were not recorded in the financial statements. The fixed assets that were reported on the

financial statements were capitalized in error or in the wrong amount and often were not removed from the financial statements after disposal or transfer. As a result, the Navy's Consolidated Statement of Financial Position was understated by $177.5 million. The Air Force Base Support business area did not accurately record, capitalize, and value fixed assets. As a result, the $5.7 million fixed assets balance may be materially misstated.

The Army Depot Maintenance Business Area did not properly account for materiel inventories valued at about $332.4 million because of inaccurate costing methods and poor record keeping. Also, about $84.8 million in intransit inventories reported in the financial statement may be invalid because the transactions are old and supporting documentation was difficult to find. Additionally, the Army Transportation inventories were valued at the latest acquisition price. The Navy DBOF physical inventories were not conducted or, when conducted, were incomplete. The Navy's DBOF unused materiel was not returned to the appropriate inventory account or recorded on financial records and stock levels were not always reviewed for excesses. As a result, the Department of the Navy's DBOF Consolidated Financial Statements contained $153.0 million in gross inventory misstatement.

DoD RESPONSE: Concur that fixed assets and inventories should be consistently valued and accurately reported on DBOF financial statements. However, before the Department can comment further, individual audit reports for the respective DoD Components must be made available for further review and comment.

TRANSACTIONS NOT EXECUTED IN COMPLIANCE WITH EXISTING GUIDANCE

- DODIG Finding: **Lack of Reconciliation.** The financial data was not reconciled to assure consistent reporting of the same information. The August 19, 1991, "Fiscal Year 1992 DBOF Financial Management Guidance," stated that disbursement and collection reports shall be reviewed and reconciled to the Statement of Transactions (SOT) before being submitted to the next reporting level. Each DFAS Center's divisions and branches are responsible for specific reports; however, The DoDIG could not identify one reporting division or branch at the DFAS Centers performing any form of reconciliation with the SOT, or with another reporting division or branch, before or after the information is transmitted to Treasury. This condition results in inconsistencies between cash reporting and financial presentation. During our visits to the DFAS Centers, The DoDIG determined that no reconciliations of Fund Balances with Treasury were performed in FY 1992, which resulted in

an unreconciled difference of $15.8 million between the DFAS Statement of Financial Position and the General Ledger. The DoDIG found the DFSC did not coordinate with the DFAS to ensure that financial data was accurate. The DFSC internal management control reviews required by the FMFIA did not determine whether subsidiary ledger accounting records were periodically verified to supporting documentation, did not properly track and report material weaknesses, and had not established procedures to describe the coordination between the DFSC and the DFAS.

DoD RESPONSE: Concur. Reconciliations should be performed. However, before the Department can comment further, individual audit reports for the respective DoD Components must be made available for review.

- DODIG Finding: **Unreliable Weekly Flash Cash Reports.** The Weekly Flash Cash Reports cannot be relied on to evaluate cash working cycle needs of DBOF. A requirement to prepare DBOF Weekly Flash Cash Reports was implemented to aid management in determining what the cash needs should be for a given time frame. The DoDIG determined that feeder reports from the business areas did not agree with reports submitted to the DoD Comptroller by the DFAS-Cleveland Center, Defense Accounting Office, Arlington, Virginia. Even though the DBOF business areas were providing the Weekly Flash Cash Reports, the reports were not reconciled and included estimates and inaccuracies that rendered them useless for management cash flow decisions.

  DoD RESPONSE: Partially Concur. Cash transactions should be reconciled daily to the disbursing officer's daily cash blotter, and DFAS Centers should not arbitrary change data submitted from the individual disbursing offices before submission to the DOD Comptroller. The content of the weekly cash reports should agree with the financial reports, except for differences in reporting periods. The Flash Cash report is intended to give management advance notice of the DBOF cash position and must be a useful tool in evaluating cash needs of the DBOF.

- DODIG Finding: **Inadequate Audit Trails.** Audit trails were not sufficient to trace voucher transactions at the sites visited. The Joint Financial Management Improvement Program's publication, "Core Financial System Requirements," January 1988, requires that systems provide audit trails that trace transactions from source documents through successive levels of summarization to the financial statements. The audit trail should also be traceable in reverse. The accounting systems at the DFAS Centers in Columbus and Indianapolis do not include document or voucher numbers for DBOF transactions. The DFAS Centers report DBOF

cash transactions to Treasury based on feeder information from disbursing offices of each Military Department. For example, at the DFAS-Indianapolis Center, the data is summarized by the disbursing offices and batch processed (daily by the Air Force and weekly for all other Services) to the DFAS Center with a batch number reference instead of a document or voucher number. A sample of 50 summarized transactions selected from the DFAS-Indianapolis Center's accounting system included more than 7,000 detailed transactions. The detailed transactions are stored on microfiche organized by disbursing offices, then by appropriation. Supporting documentation for the detailed transactions is held on site for 6 months, then forwarded to the funding activity. The Army Audit Agency found that the lack of an audit trail made the verification of account balances difficult at the audit sites. The Air Force Transportation business area did not have a system in place to accurately capitalize property, plant and equipment. In addition the Air Force Audit Agency was unable to substantiate $1.07 billion of channel revenue, $998.9 million of military personnel expenses, and $339.9 million of property, plant and equipment at the Air Force Transportation business area due to an incomplete audit trail. Also, disbursements of $546.0 million were made to commercial carriers without evidence from the carriers that the services were rendered.

DoD RESPONSE: Nonconcur. This finding presumes that the entire DBOF transaction data base is transmitted through successive levels of consolidation for financial reporting purposes. Within current accounting systems, individual transactions retain an audit trail through the first level of summarization. Subsequently, audit trails of summarized amounts retain audit trails through each level of consolidation.

- DODIG Finding: Lack of Uniform Accounting Systems. The accounting systems in use by the DFAS Centers do not provide consistency in financial reporting or comparability of information on operations for the DBOF. The CFO Act, November 15, 1990, requires an agency Chief Financial Officer to develop and maintain an integrated agency accounting and financial management system. Such systems are to provide for complete, reliable, consistent, and timely information prepared on a uniform basis and responsive to the financial information needs of agency management. The DFAS Centers are using existing accounting systems to provide Service-unique information, while the DBOF reporting requirements are the same for each Service. Each of the DFAS Centers has developed unique computer programs to summarize information for reporting to the DBOF. The summarized information must be collected from several Service-unique sources, which results in a further lack of

comparability for data received for the DBOF from the DFAS Centers. The DeCA did not have an effective reporting system that systematically summarized financial information. The DoDIG found no documented procedures for the DFSC to determine which general ledger accounts were used to develop the various account classifications on the financial statements. The DoDIG determined that DFAS personnel had to crosswalk Defense Logistics Agency general ledger accounts to the DoD uniform chart of accounts, then crosswalk the DoD accounts to the account classifications on the financial statements. The Army's Depot Maintenance and Transportation business areas, integrated general ledger systems were not used to produce the Army's FY 1992 financial statements. Instead, reports from the Departmental Budget and Reporting System were relied on for preparing financial reports. Similarly, the Air Force Transportation business area did not have a fully integrated double-entry accounting system. Information was gathered from automated and manual systems to create a consolidated general ledger. The procedures used to create this general ledger were not documented, and there was no assurance that all transactions were recorded. The Air Force Supply Management automated accounting system was not in place to collect and report expenses as required and the accounting systems did not generate sufficient and suitable accounting data to permit the review and certification of fiscal year financial statements. These conditions exist because the Standard General Ledger accounts have not been incorporated into the DFAS accounting systems.

DoD RESPONSE: Concur in principle. A uniform application of general ledger balances is the preferred method of consolidating and preparing financial statements. The finding does not, however, present any evidence that the Defense Finance and Accounting Service centers were erroneous in their application of procedures in the preparation of the DBOF financial statements.

- **DODIG Finding: Lack of Standard General Ledger.** The U.S. Government Standard General Ledger (SGL) has not been fully implemented by the DFAS for the DBOF business areas as required by the GAO's "Policy and Procedures Manual for Guidance of Federal Agencies, Title 2, Accounting." The DoDIG identified at least seven different general ledger structures in use by DBOF activities. The SGL is intended to standardize Federal accounting and to meet the basic Federal financial statement and budget execution reporting requirements. The Military Services and the DoD Components are using Service-unique charts of accounts and are crosswalking the financial data from the activities' general ledger accounts to the SGL for preparation of management reports and financial statements. The lack of a uniform general ledger structure within the DBOF unnecessarily

increases the potential for accounting errors and increases the level of effort required to prepare and audit financial statements or routine reports for the use of other Government parties, such as the Treasury and the OMB. Since the crosswalks in use do not always have a one-for-one relationship to the SGL, transactions are not properly recorded and accounted for to permit the preparation of reliable financial statements and to maintain accountability over assets. In addition, the general ledger accounts in use at the DFAS Centers do not adequately record the level of detail required in the DoD Comptroller memorandum, "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992. In FY 1992, only one of the DBOF activities, the DeCA, Resale Stocks business area, used the DoD Uniform Chart of Accounts, which is equivalent to the SGL. The Defense Information Service Agency Information Services business area has contracted with the accounting firm of KPMG Peat Marwick to convert its accounting system to the SGL for FY 1993.

DoD RESPONSE: Concur in principle. The finding implies that financial statements can be prepared from the U.S. Government Standard General Ledger. This will be true when general ledgers are populated by transactions that have been modeled to support all data and process requirements, and these transactions are resident in data base applications.

INSPECTOR GENERAL, DEPARTMENT OF DEFENSE,
"DRAFT REPORT ON INTERNAL CONTROLS AND COMPLIANCE WITH LAWS AND REGULATIONS FOR THE DEFENSE BUSINESS OPERATIONS FUND (DBOF) FINANCIAL STATEMENTS FOR FY 1992"
(PROJECT NO. 2FG-0028)

DEPARTMENT OF DEFENSE COMMENTS

* * * * *

FINDINGS

PART III COMPLIANCE WITH LAWS AND REGULATIONS

- DODIG Finding: Budget and Accounting Procedures Act of 1950 and Title 2. Accounting systems for the DBOF do not meet accounting system requirements of GAO's "Policy and Procedures Manual for Guidance of Federal Agencies, Title 2, Accounting" (Title 2). Under the Budget and Accounting Procedures Act, the head of each Federal agency is responsible for establishing and maintaining adequate systems of accounting and internal controls. The Act also requires that these systems conform to the accounting principles, standards, and related requirements prescribed by the Comptroller General. Appendix III to Title 2 prescribes accounting system standards and requirements that agency heads must observe in establishing, maintaining, and reporting on their systems of accounting and internal controls. This includes a requirement that accounting systems be maintained on an accrual basis and use the United States General Ledger chart of accounts and meet "Core Financial System Requirements," January 1988, the Joint Financial Management Improvement Programs. The systems must incorporate adequate audit trails and double-entry accounting. Further, systems should include, for each appropriation or fund, accounts that provide appropriation records on obligations incurred and liquidated to assist in controlling expenditures and disbursements and in reporting the status of appropriations and funds. Our audit identified material instances where accounting systems were not in compliance with these requirements. These instances of noncompliance are discussed in detail in Part II, Internal Controls, sections on Lack of Standard General Ledger, Inadequate Audit Trails, and Lack of Uniform Accounting Systems. Additionally, The DoDIG found that the DFAS did not disclose the value of the use of the facilities at three of the five DFAS Centers (which The DoDIG estimated to be $27.0 million) as required by Title 2. The Centers were provided to the DFAS at no cost in FY 1992.

  DoD RESPONSE: Nonconcur. The direction from the Office of Management and Budget in OMB Bulletin 93-02 is that pending issuance of final accounting standards, the Federal

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Accounting Standards Advisory Board (FASAB) has recommended, and the three principals have agreed to, the following interim guidance:

> in order to provide a benchmark for preparing financial statements presented for audit, executive agencies should continue using the applicable accounting standards (i.e., those contained in agency accounting policy, procedures manuals, and/or related guidance) now in effect for the preparation of their financial statements, pending FASAB recommendations and JFMIP Principals' adoption of Federal accounting standards.

- DODIG Finding: **Chief Financial Officers Act of 1990.** The Office of the DoD Comptroller, did not fully comply with OMB Bulletin No. 93-02, which implements the Chief Financial Officers Act (CFO Act). The financial statements were not submitted to the Director, OMB, by the required date, and the financial statements were incomplete. The DoDIG believes that several factors contributed to the late and incomplete submission of the financial statements.

  - Many of the DFAS personnel tasked with preparing financial statements had no prior experience with preparing financial statements.
  - The accounting systems used were not always able to generate accurate accounting information in the proper form to prepare the statements, so accounting personnel had to rely on manual methods, electronic spreadsheets, and estimates to prepare the statements.
  - Final OMB guidance on form and content of the financial statements was not issued until after the end of the fiscal year.
  - Management indecision during the year as to who was responsible for preparing the statements and at what reporting levels they should be prepared impeded planning for statement preparation.

  OMB Bulletin No. 93-02 requires each agency to prepare, for each reporting entity under the CFO Act, an Overview of the Reporting Entity, Principal Statements, Combining Statements (if applicable), and Supplemental Financial and Management Information. The Notes to the Principal Statements are a required part of the Principal Statements. Section 3515 of the Act also requires each agency to submit its annual financial statement no later than March 31 of the following year. The Office of the DoD Comptroller did not provide the financial statements to the OMB until April 7, 1993. The

statements were incomplete because they lacked the required Notes to the Principal Statements and the Supplemental Financial and Management Information. These are integral parts of the financial statements that are necessary to fairly present the results of operations.

<u>DoD RESPONSE</u>: Partially concur. The unaudited financial statements were provided to the Office of Management and Budget on April 1, 1993. The principal statements were presented without the applicable "Notes" and supplemental information. However, the DoD Component consolidating and business area financial statements were presented with the appropriate "Notes" and supplemental information.

DEBT COLLECTION ACT

- <u>DODIG Finding</u>: **Debt Collection Act.** Quarterly and annual reports to the Treasury on Accounts and Loans Receivable Due from the Public (Standard Form 220-9) were not accurately prepared. Quarterly reports were understated by about $60.0 million because the DFAS did not obtain feeder reports for all of the DBOF business areas. The annual report was overstated by $4.7 million due to a $29.3 million overstatement for the DBOF business areas and a $24.5 million understatement for the Air Force business areas. The errors in the annual report occurred because the DFAS did not reconcile the amounts reported to Treasury with the Accounts Receivable, Net Non-Federal, account shown on the financial statements and because a $12.2 million error identified by the DFAS was not corrected before submission of the report to Treasury. The DoDIG also found that no systems were in place to manage the collection of debts from contractors.

The Debt Collection Act of 1982 (Public Law No. 97-365) expanded the rights given to Federal agencies by the Federal Claims Collection Act of 1966. The Debt Collection Act authorizes Federal agencies to assess interest, penalties, and administrative charges on debts owed by the public. The Debt Collection Act also authorized the Government to use such tools as credit bureaus and debt collection agencies and authorized the assessment of interest penalties and administrative costs against debtors with respect to debts owed to the United States. A debt is considered delinquent if it has not been paid by the date specified in the agency's initial demand letter, unless satisfactory payment arrangements have been made by that date, or if, at any time thereafter, the debtor fails to satisfy his obligations under the payment agreement. Once the penalty has been assessed and the appeal period has lapsed, interest, penalties, and administrative costs should be added to the penalty amount.

Schedule 220-9, Report on Accounts and Loans Receivable Due From the Public, is required on an annual basis by the Treasury Financial Manual for all reporting entities, including those with no receivables. Entities with receivables of less than $50.0 million are required to submit annually, and entities having receivables of $50.0 million or more are required to report quarterly. OMB Bulletin No. 93-02 requires that amounts shown as Accounts Receivable, Net - Non-Federal, agree with information on the SF 220-9 report. The DFAS is responsible for collecting debts and charging the prescribed interest, administrative fees, and penalties for the DBOF and preparing and submitting the required reports to Treasury.

DoD RESPONSE: Concur in principle. However, before the Department can comment further, individual audit reports for the respective DoD Components must be made available for review.

- DODIG Finding: Quarterly Reports to Treasury. Managers for four of the five Air Force business areas did not submit the required feeder reports to the DFAS-Cleveland Center, Defense Accounting Office, Arlington, Virginia, needed to prepare the quarterly DBOF consolidated SF 220-9 Reports on Loans and Receivables Due from the Public. As a result, the DoDIG estimated that quarterly reports for second and third quarters FY 1992 was understated by about $60.0 million. The DoDIG was unable to review the feeder reports for the first quarter because the Defense Accounting Office had lost the reports. Responsible personnel at the DFAS-Denver Center did not submit the feeder reports because they had misunderstood the $50.0 million reporting threshold; they did not submit the required information because the business area's receivables were below $50.0 million. The Defense Accounting Office prepared a consolidated report and the $50.0 million threshold applied to the DBOF as a whole rather than the individual business areas. Additionally, the consolidated quarterly reports were understated. Also, the Defense Accounting Office should have ensured that all business areas had been included in the consolidated reports before submitting the reports to Treasury.

  Also, SF 220-9 feeder reports for all five of the Air Force business areas did not report the collection of interest, penalties, or administrative costs. The trial balances for these business areas did not indicate that such items were being collected as required by the Debt Collection Act.

  DoD RESPONSE: Concur in principle. However, before the Department can comment further, individual audit reports for the respective DoD Components must be made available for review.

- DODIG Finding: Annual Reports to the Treasury. The amounts shown as Accounts Receivable, Net Non-Federal, on the financial statements for the DBOF did not agree with the amounts submitted to the Treasury on the SF 220-9, Report on Loans and Accounts Receivable Due from the Public for Fiscal Year 1992. This occurred because the two amounts had not been reconciled as required by OMB Bulletin No. 93-02. Table 1. shows the differences between the two amounts.

Table 1 Variances Between Accounts Receivable Due from the Public as Shown on the DBOF Financial Statements and DBOF Accounts Receivable Reported to Treasury on SF 220-9 Annual Report

DoD Component	Financial Statements (Millions)	SF220-9 Reports (Millions)	Statements Overstated (Millions)	Statements Understated (Millions)
Army	$ 7.6	$ 7.9	$ 0.0	$ .3
Navy	117.7	117.5	.2	0.0
Air Force	93.0	117.5	0.0	24.5
Defense	125.6	96.3	29.3	0.0
DISA 1/	.6	.6	0.0	0.0
DeCA 2/	124.7	124.7	0.0	0.0
Total	$469.2	$464.5	$29.5	$24.8

1/ Defense Information Systems Agency
2/ Defense Commissary Agency

DoD RESPONSE: Concur. It is noted that the net overstated amount of $4.7 million is approximately 1 percent of the total.

- DODIG Finding: Contractor Debts. Contractor debts are currently being managed by the DFAS-Columbus Center. At the time of our audit, no system had been implemented to track debts from contractors. As a result, the DoDIG could not determine whether such debts were being properly managed and reported. The DFAS-Denver Center is developing a system to manage contractor debt and expects to install the system during December 1993. The DoDIG examined the documentation for the proposed system and it appeared to meet requirements of the Debt Collection Act.

DoD RESPONSE: Concur.

- DODIG Finding: Follow-up on Audit Report No. 92-021. Although the DFAS agreed to centralize management of DoD's debt collection function and to develop uniform operating

procedures, such procedures had not been issued. Specifically, the DFAS agreed by the end of FY 1992 to:

- establish time frames for carrying out each procedure in the debt collection strategy;
- require collection activities to periodically report whether they meet the time frames.
- identify and write off all delinquent debts that are unlikely to be collected; and
- require aggressive pursuit of all delinquent debts and standardize the implementation of all procedures required by laws and regulations, including procedures of assessing interest, penalties, and administrative fees and for reporting uncollectible debts to the Internal Revenue Service.

As of the end of our field work, April 30, 1993, these uniform operating procedures had not been issued.

DoD RESPONSE: Concur. The Defense Finance and Accounting Service has developed standard migration system called the Defense Debt Management System which is expected to satisfy the requirements of the Debt Collection Act. This system is expected to be implemented in mid-1993. (See next finding.)

- DODIG Finding: **Improvements to Debt Collection.** A standard debt collection system called the Defense Debt Management System has been developed by the DFAS-Denver Center and should be implemented at all DFAS Centers by July 30, 1993. The system features on-line processing, single-source data entry, automated interfaces from pay systems from which debts originate, and interfaces with other organizations. Documentation for the system showed that it will satisfy requirements of the Debt Collection Act. In addition, the DFAS has arranged for a centralized lockbox for its debt collections. A lockbox is a collection and processing service provided by a financial institution to accelerate the flow of funds to the Treasury's General Account. This service includes collecting the agency's mail from a specified post office box; sorting, totaling, and recording the payments; processing the items; mailing the deposit; and transferring the funds. Management estimated that the lockbox would result in savings of about $8.0 million annually to the DFAS.

DoD RESPONSE: Concur.

OTHER FINDINGS

- <u>DODIG Finding</u>: DoD Accounting Manual. Air Force Supply Management - General Support Accounting Adjustments were not properly approved and documented; shipment discrepancies were not properly documented; interfund accounts payable transactions were not processed in the month they occurred; actual sales were not reported in financial statements; payments to contractors were not properly documented; consignments were not separately disclosed in financial statements and accounting adjustments were not approved and documented as required by the DoD Accounting Manual.

  <u>DoD RESPONSE</u>: Concur in principle. However, before the Department can comment further, individual audit reports for the respective DoD Component business area must be made available for review to determine if these are overall traits or isolated incidents.

- <u>DODIG Finding</u>: Department of Defense Appropriations Act, 1992, Section 8121. Policy managers for the DBOF did not take adequate steps to establish a separate subaccount for DBOF capital reserve funds as required by the Defense Appropriations Act. The DBOF's Capital Budget for FY 1992 was $1.1 billion. The DoD Comptroller issued capital asset guidance on July 21, 1992, which established new general ledger accounts to distinguish operating funds from capital asset funds. The guidance, however, was not issued until about 8 months after the law became effective; the new accounts have not yet been established by the business area managers; and it is questionable whether the business areas can implement the guidance since only 1 of the 33 business areas is using the Standard General Ledger (see Part II, Internal Controls, Standard General Ledger). Additionally, the DoDIG found the accuracy of the Monthly Report of Operations (DD Form 1307) used to track capital asset purchases questionable.

  The DoD Appropriations Act, P.L. 102-172, Section 8121(d), effective November 26, 1991, required that a separate subaccount be established for recording and reporting all capital asset transactions. The subaccount would separate operating funds (funds used for all transactions that are not related to the acquisition of capital assets) from capital asset funds. A capital asset is a long-lived asset such as buildings, equipment, and improvements. Capital asset transactions are those that generate funds and recognize revenue from capital asset depreciation, as well as those that generate minor construction surcharges included in customer rates, obligations for capital asset purchases, and outlays for capital assets. The money for future capital asset investments is generated from

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depreciation and surcharges included in customer rates. A capital surcharge was applied by the DoD Comptroller for FY 1992 as a means of providing the initial seed money for future capital asset investments. This initial seed money totaled $1.3 billion. The DoD Comptroller issued guidance for capital asset accounting in July 1992, which established new general ledger account codes in the DoD Uniform Chart of Accounts (equivalent to the U.S. Standard General Ledger) to segregate capital asset funds from operating funds.

Each fiscal year, each business activity's annual operating budget identifies the capital assets to be purchased during the year and the ceiling limitations for those assets. The business activities are permitted to purchase capital assets as long as they do not exceed their capital budget ceiling limitations. It was assumed by the business activities that since the capital assets were in their capital budgets, the money was available to be spent on capital investments. Therefore, operating funds were used, along with the money that was collected from depreciation and surcharges for capital assets, during the fiscal year.

The capital asset guidance was not issued in time to allow the business activities to properly account for capital asset transactions. The accounting systems used by the activities were not updated to include the new general ledger account codes; therefore, operating funds and capital monies were not separately recorded. Until the capital reserve subaccount is established in the various accounting systems used by the Fund or an alternate strategy to separate the funds is developed, the improper use of operating funds will continue.

The Monthly Report of Operations is a cumulative summary operating report used by the Office of the DoD Comptroller. Until early FY 1992, each DoD Component having one or more industrial fund activity groups were required to submit the Monthly Report of Operations, and DoD Components having one or more stock fund groups were required to submit the Monthly Management Report (DD Form 1302). Since December 1991, however, only the Monthly Report of Operations has been used to monitor operations within the DBOF.

The report is similar in design to that of an income statement, depicting revenues, expenses, and net results. Revenue is divided into three areas that identify the source of the activities' revenues: operations, surcharges, and other revenue. Expense is divided into six categories which, when totaled, equal the cost of sales. Net results, net operating results, and unfunded costs are also parts of the report. In addition, two other items were added to the report to indicate the status of capital asset investments. Activities are to report the amount obligated for capital asset purchases for the year and net outlays for capital

assets for the year to date. Chapter 95 of the DoD Manual 7220.9-M DoD Accounting Manual provides guidance for preparing the Monthly Report of Operations.

DoD RESPONSE: Partially concur. The requirement to segregate revenue into separate categories for capital asset surcharges and the reporting of capital obligations and outlays on the Report of Operations was identified in the Defense Finance and Accounting Service memorandum "Defense Business Operations Fund (DBOF) Reporting Requirements" on October 11, 1991. The Report of Operations (AR 1307) and the Monthly Management Report (AR 1302) are both used to monitor operations of the DBOF. These reports were required by the same DFAS October 11, 1991 memorandum.

- DODIG Finding: **Monthly Report of Operations.** The required financial information for the Monthly Report of Operations was inconsistent, incomplete, and inaccurate. The guidance in the DoD Accounting Manual for the preparation of the report was outdated and did not provide a crosswalk to the general ledger accounts. As a result, the DoD was unable to effectively track the true cost of operations or monitor the capital budget.

The current guidance states that the report is to be submitted within 45 days after the end of each month. If all financial data is not available at the required submission time, activities are to "provide the best estimate of any incomplete data and identify data as estimated." The guidance in the DoD Accounting Manual does not provide a crosswalk indicating the general ledger accounts that should be used in preparing the monthly report. The financial data used to prepare the report is supposed to be taken from the same accounting systems that generate the trial balances used in preparing the year-end financial statements for each of the business activities. The DoDIG performed a comparison of the Purchases of Property, Plant and Equipment shown on the FY 1992 financial statements with the Obligations and Net Outlays for capital equipment. Our comparison, shown in Table 2., identified significant differences between the two reports.

Table 2
Comparison of the Statement of Cash Flows with Obligations and Net Outlays by Military Component ($ millions)

Component	FY 1992 Financial Statements -- Statement of Cash Flows 1/	Monthly Report of Operations Obligations and Net Outlays	Difference
Army	$ 519.1	$ 106.0	($413.1)
Navy	86.6	205.0	118.4
Air Force	3.2	403.0	399.8
DeCA	0.0	2.0	2.0
DISA	0.4	0.0	(0.4)
DLA	85.7	298.0	212.3
Totals	$ 695.0	$1,014.0	$ 319.0

1/ These amounts were derived from line 17, "Purchases of Property, Plant, ad Equipment," in the Cash Flows from Non-Operating Activities section of the Statement of Cash Flows.

These amounts should be equal if the same general ledger accounts are used for both financial documents. The Monthly Report of Operations is used by the DoD Comptroller to determine if each business area is operating within its operating and capital budgets. The DoDIG questions, therefore, whether the DoD Comptroller should authorize estimates to be used for the report.

At the present, personnel in the DoD Comptroller's Office agree that the financial information is not very reliable, especially the information received from the old stock fund business activities, since these areas were not required to prepare this form until the early part of FY 1992. As an extra precaution, the DoD Comptroller requires business activity managers to verbally inform that office if the manager anticipates that its business activity is going to exceed its budget. In addition, Headquarters, Defense Finance and Accounting Service, is in the process of revising the guidance on the preparation of the Monthly Report of Operations. This revised guidance will include a crosswalk indicating the general ledger accounts used for each line on the report. Until this guidance is issued, however, preparation of the monthly report will continue to follow the current guidance in the DoD Accounting Manual.

DoD RESPONSE: Nonconcur. The finding references information 18 months out of date and misleads the reader to believe that the Department has not taken steps to correct known deficiencies. The Defense Finance and Accounting Service revised the guidance on "Defense Business Operations Fund (DBOF) Reporting Requirements" on October 11, 1991.

The due date for the Accounting Report (AR)1307 Monthly Report of Operations was changed to 15 working days following the report month. On August 11, 1992, the Comptroller advised the DoD Components that deficiencies had been found in the monthly reports and required corrective actions to be completed in the business area for August 1992 reporting.

- DODIG Finding: Federal Manager's Financial Integrity Act of 1982. The DeCA did not comply with FMFIA requirements. Additionally, DFAS and Air Force financial managers either did not accomplish or did not perform adequate FMFIA detail and general reviews in accordance with FMFIA.

  DoD RESPONSE: DoD is not able to concur or nonconcur at this time. A more in-depth assessment of the the finding is required before the Department can comment.

- DODIG Finding: OMB Bulletin 93-02. The audit of Defense Business Operations Fund Depot Maintenance, Army (Army Audit Agency Project N2-471C) found that the DFAS did not follow DoD guidance on form and content of FY 1992 financial statements when classifying Army Depot Maintenance inventories.

  The audit of the Fiscal Year 1992 Consolidating Financial Statements of the Department of the Navy's Defense Business Operations Fund (Project 93-0027) found that financial statements were inaccurate. For example, balances for Material-in-Transit and Progress Payments were not reported, financial records were adjusted to agree with the financial statements, negative balances in inventory records were not corrected and were included on the financial statements, and financial records for the Military Sealift Command did not accurately support and present accrual balances.

  DoD RESPONSE: Nonconcur. The finding is incorrect and misleading in its conclusion of the audit of the Navy Defense Business Operations Fund (Project 93-0027). The Naval Area Audit Service audited lines 1.g, "Inventories Held For Sale, Net"; 2.b, "Inventories Not Held For Sale;" and 2.c, "Plant, Property, and Equipment, Net" and line 4., "Funded Liabilities" of the Navy DBOF Statement of Financial Position. The audit did not cover the remaining 16 lines items of general ledger balances on the Navy Consolidating Statement of Financial Position; nor did the audit encompass the Navy Consolidated DBOF Statement of Operations (and Changes in Net Position); the Statement of Cash Flows (Indirect)" or the "Statement of Budget and Actual Expenses."

- DODIG Finding: Real Property Ownership Under the Military Construction Codification Act. Real property is being shown as an asset of the DBOF and depreciation for real property is being shown as a source of revenue, even though the Military Construction Codification Act (P.L. 97-214) precludes the ownership of real property by Defense agencies. This occurred because of the guidance on criteria for capitalization of assets issued by the Office of the DoD Comptroller on July 21, 1992, based on Section 8121 of P.L. 102-172. As a result, assets pertaining to real property were overstated by $2.3 billion and depreciation expenses for real property were overstated by about $135.0 million.

  The applicable provisions of P.L. 97-214 Were implemented by 10 U.S.C. § 2682. The provisions preclude the ownership of real property:

  > "The maintenance and repair of a real property facility for an activity or agency of the Department of Defense (other than a military department) financed from appropriations for military functions of the Department of Defense will he accomplished by or through a Military Department designated by the Secretary of Defense. A real property facility under the jurisdiction of the DoD which is used by a activity or agency of the DoD (other than a Military Department) shall be under the jurisdiction of a Military Department designated by the Secretary of Defense."

  The DBOF was established under Section 8121 of P.L. 102-172. The Act transferred to the Fund all assets under the provisions of 10 U.S.C. § 2208.

  Based on this Act, the Office of the DoD Comptroller issued the DBOF guidance for Capital Asset Accounting, July 21, 1992. The guidance states that ownership of capital assets used by a fund activity in providing goods or services must be recognized in the property and financial records of that fund activity. Capital assets include, but are not limited to, physical, plant and property (including Government-owned facilities, property, and improvements to property acquired under a capital lease), equipment, and software. Additionally, the Fund activities are required to charge a depreciation expense on their capital assets.

  The review of the financial statements disclosed real property shown as an asset of the DBOF. The assets of the former Air Force and Army industrial and stock funds have been capitalized to the Component business areas of the Fund. Because the DBOF is a Defense fund, the DoDIG believes that P.L. 97-214 precludes ownership of real property by the DBOF. Also, the DoDIG believes P.L. 102-172

did not specifically supersede P.L. 97-214. Accordingly, the DoDIG believes that capitalization or depreciation of an asset which is not legally owned by the DBOF would not be appropriate accounting procedures. If the DBOF managers wish to include the costs of real property in their results of operations, however, this can be accomplished through the use of rental agreements (interservice support agreements) with the DoD Component that legally owns the real property.

DoD RESPONSE: Partially concur. DBOF financial statements identify real property as an asset of the fund. The inclusion of real property items, and related depreciation is intended to reflect the full range of assets and costs associated with the operations of DBOF activities. Before action regarding the above finding is taken the Office of the DoD Comptroller will seek the advice of the Office of General Counsel.

- DODIG Finding: **National Defense Authorization Act for Fiscal Years 1992 and 1993, Section 316.** Section 316 of the Defense Authorization Act prohibits the addition of other functions, activities, funds, or accounts of the DoD to the Defense Business Operations Fund. During FY 1992, two new activities were added to the DBOF, the Defense Information Technology Services Organization (DITSO) and the Joint Logistics Systems Center (JLSC). The DoDIG believes making these additions violated the prohibition. The DITSO was established to provide information technology services for the DoD Components within the Fund. The JLSC was established to oversee the development of systems changes for the supply management and depot maintenance business activities of the Fund.

  The National Defense Authorization Act for FYs 1992 and 1993 authorized appropriations for those fiscal years for military activities of the DoD, military construction, and defense activities of the Department of Energy. Section 316 of the act provides certain limitations on the use of the DBOF. One such limitation prohibits the addition to the Fund of other functions, activities, funds, or accounts of the DoD.

  DoD RESPONSE: Nonconcur. The two new organizations did not represent new functions, activities, funds or accounts; but rather, were a reorganization of activities already within the fund.

- DODIG Finding: **Prompt Payment Act.** The Prompt Payment Act was enacted as P.L. 97-177 on May 21,1982, and was amended on October 17, 1988, as P.L. 100-496. The Prompt Payment Act requires agencies to make payments on time, to pay interest penalties when payments are late, and to take

discounts only when payments are made on or before the discount date.

Prior audits of The Prompt Payment Act identified that Finance and Accounting Offices were not complying with OMB Circular A-125, all early and late payments were not being reported, discounts were offered and not being taken, interest penalties were being incurred, interest was not being paid on late payments, and payments were issued without proper receiving reports. The DoDIG identified that in FY 1992, the DFAS-Columbus Center was paying invoices late, payments were being paid after the due date, discounts were not being taken, interest penalties were being incurred, and interest was not being paid on late payments. The DFAS-Columbus Center reported 1.7 million invoices totaling $61.3 billion subject to prompt payment. Of those, 74,000 invoices valued at about $2.8 billion were reported by the DFAS as paid late. Interest on the late payments was reported at $9.0 million. In addition, the DoDIG found that the DeCA did not comply with provisions of the Prompt Payment Act because it did not take advantage of offered discounts.

DoD RESPONSE: Concur. However, the review of a single DFAS center, and a single DBOF business area, would not appear to provide sufficient evidence to conclude that finance and accounting offices are not complying with OMB Circular A-125.

- DODIG Finding: **Instances of Non-compliance with DoD Accounting Policies.** A DoD memorandum, Interim Stock Fund Policies, dated July 9, 1990, was implemented in FY 1991 and established the Cost of Operations Division (COD) that became part of the Air Force Supply Management business area of the Defense Business Operations Fund in FY 1992. The memorandum required the COD to account for all overhead costs incurred by Air Force Supply Management and Distribution Depots business areas. The costs include civilian and military personnel payroll expenses, travel, supplies, utilities, and depreciation. The audit of Compliance with Laws and Regulations and Management Issues Related to Air Force Supply Management and Distribution Depot, FY 1992 Financial Statements (Project 93068001) found that Air Force did not properly identify and assign COD positions to permit the evaluation of actual costs associated with the management of inventory control point and distribution depot activities. The DoDIG also found Air Logistics Centers did not compute reimbursements to the military pay appropriation as required by the DoD Memorandum, Interim Stock Fund Policies, July 9, 1990.

  Our audit of Defense Finance and Accounting Service Revolving Fund Consolidating Financial Statements of the

Defense Business Operations Fund for FY 1992 (Project 2FG-2004) found that the DFAS did not develop depreciation schedules for capital assets based on established useful life criteria. Also, assets had not been transferred to the central design activities and information processing centers when capitalized, nor had assets been transferred to the Defense Information Technology Services Organization when it was established during FY 1992 as required by DoD Accounting Manual 7220.9 and memorandum guidance from the DoD Comptroller, "Capital Asset Accounting Guidance for the Defense Business Operations Fund," July 21, 1992.

DoD RESPONSE: Concur.

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